OTA WORKSHOP ON CARGO POLICY

December 3 and 4, 1984

PANELISTS' PRESENTATIONS AND SUMMARY OF DISCUSSION

Produced in conjunction with the OTA Background Paper,

Alternative Approaches to Cargo Policy:
A Supplement to An Assessment of Maritime Trade and Technology

U.S. Congress

Office of Technology Assessment

August 1985

These working papers have been neither reviewed
nor approved by the Technology Assessment Board.

36
J952-34

PANEL ON CURRENT POLICY INITIATIVES

December 3, 1984

PANELISTS

Charles Angevine
Department of State

Deborah Christie
Department of Defense

Robert Ellsworth
Federal Maritime Commission

William Johnson
Department of Commerce

Arnold Levine
Department of Transportation

Kay McLennan
Department of Agriculture

Lewis Paine
Department of Transportation

TOPICS FOR DISCUSSION

1. Trends in maritime trade, trading patterns, and shipping services; current policy initiatives involving the interaction of trade and shipping.
2. Present cargo preference regulations and their effects, including trends in U.S. policies to promote U.S. exports.
3. Current initiatives and responses to international cargo policies, such as the UNCTAD Liner Code and bilateral agreements with major trading partners.
4. Current trends in the use of new Shipping Act authority to gain cargo access and the effect of regulatory policy on U.S. cargo shares.
5. Impacts of military readiness requirements on cargo policies or U.S. position in trade and shipping.

SUMMARY OF DISCUSSION

At the first workshop panel, participants from Federal agencies discussed current initiatives in cargo policy. The agencies represented included the Departments of State, Agriculture, Transportation, Commerce, and Defense, and the Federal Maritime Commission. The panelists presented an optimistic outlook for both U.S. shippers and the maritime industry. They stressed that their programs were directed toward goals of maximum flexibility for shippers along with access to cargo for U.S. carriers. A common theme expressed was "open market competition." On the international level, the panelists believed it important to protect U.S. vessels from unfair practices in order to meet the goals of access and competition.

Shipping Act of 1984

Several participants stressed the role of the 1984 Shipping Act in enabling U.S. interests to overcome barriers to market access in international liner trade. The Act allows conferences to establish intermodal rates, giving shippers the advantage of a through bill of lading. It also requires the right of independent action for any individual conference member, requiring a maximum of 10 days notice prior to such action. Shippers' associations are authorized, although antitrust exemption does not extend to them. The rate-approval process required by FMC is considerably accelerated and simplified.

The rights of all carriers in U.S. trades for protection against discrimination is provided. The Act retains section 19 of the Merchant Marine Act of 1920, under which the tariffs of any country's vessels may be suspended, effectively excluding them from U.S. trades. Provisions of the Controlled Carrier Act of 1978 are also retained in the new Act. Under this provision, action may be taken against controlled carriers of any flag which unfairly compete by offering less than compensatory rates. Finally, section 13(b)(5) of the new Act gives FMC power to suspend the tariff of any carrier in U.S. trade if the country whose flag it flies, or the commercial practices of the carrier, unduly impair the access of U.S. carriers as cross-traders in foreign-to-foreign trade. Several participants stressed the importance of this latter provision, which they viewed as vital in protecting U.S. carriers against certain cargo-sharing schemes in effect around the world.

Cargo Preference

There was considerable discussion of U.S. cargo-preference laws and policies. The stated Administration position is that current laws should be enforced, but that no expansion of preference should occur. Cargo-preference requirements on agricultural products received significant attention from the group. Under the Cargo Preference Act of 1954 (P.L. 83-664), U.S. food assistance to less developed countries (LDCs) is subject to a 50-percent U.S. carrier reservation. USDA, which manages the preference requirements for these P.L. 83-480 Title I (concessionary sales) shipments, cited a transportation differential cost of $120 million paid for U.S.-flag carriage of food assistance cargoes in 1982. The cost differential was $65 million in 1983 and $76 million in 1984. Comparable detailed statistics are not available for the Title II (gifts of food) shipments, whose preference requirements are monitored by AID.

The panelists pointed out that while one-third (by tonnage) of all U.S.-flag waterborne shipments are preferential, only 4 to 8 percent of total liner shipments are preference cargoes. In the liner sector, there is generally no differential within conferences, where set rates apply to all carriers, notwithstanding flag. Of course, this is tempered by the situation in U.S. trades where independent action is encouraged and a number of nonconference carriers operate. It should be noted, however, that in some instances an agricultural commodity rate may be "opened" by the conference, which means that a conference-wide rate does not apply.

It is in the bulk area, where U.S. operating costs average two to three times those of certain foreign competitors, that the cost differentials are significant. However, U.S. bulk carriers are utterly dependent upon preference shipments for their survival. On the other hand, panelists also pointed out that the U.S. bulk fleet is modernizing significantly. A MarAd study of the large Egyptian program showed that in 1981, 61 percent of P.L. 480 shipments were on bulk carriers over 22 years old, while in 1984, 63 percent of shipments were carried on vessels 5 years old or under. This does not imply that the U.S.-flag bulk fleet is nearing profitability. A severe depression exists worldwide in bulk shipping, and even the lowest cost competitors are failing to cover their costs.

Cargo Reservation

The issue of cargo reservation, whether unilateral, bilateral, or multilateral, was raised by several panel members. Flexibility of approach is perceived by several panel members as essential in assuring U.S. interests. FMC has recently instituted or completed investigations into the Venezuelan, Brazilian, Philippine, and Argentine trades based on allegations of discrimination against U.S. or third-flag carriers and shippers. Panelists stated that the real threat to U.S. interests is foreign government intervention, rather than commercial efforts at cargo sharing.

Most panelists also felt that the UNCTAD Liner Code has not been as detrimental thus far as was widely feared. Some indicated that the potential for real harm from UNCTAD Liner Code provisions exists only where U.S. carriers are cross-traders in a foreign-to-foreign trade. Should that occur, section 13(b)(5) of the Shipping Act of 1984 allows the FMC to intervene in U.S. trades to prevent such discrimination in foreign-to-foreign trades. The overall opinion of the panel was that the UNCTAD Liner Code does not pose much direct threat to U.S. carriers. Were a bulk code to be implemented, the effect on world trade would be much greater, but this is not regarded as an imminent possibility.

Some panelists believed that a significant problem exists in negotiations between the United States and its trading allies in Europe and Japan regarding cargo access. Over the past 3 years, the Consultative Shipping Group (CSG) has met with the United States several times in an attempt to coordinate resistance to cargo sharing. The United States has steadily opposed the UNCTAD Liner Code, while some of its allies have ratified the Code (albeit with the Brussels Package reservation).[1] At the same time, however, the United States has discussed bilateral agreements with several LDCs in response to threats of unilateral cargo reservation. Both sides, in short, perceive anticompetitive actions on the part of the other, while at the same time recognizing that coordination and cooperation are in the best interests of all parties.

Defense-Related Issues

While most of the panel's allotted time was spent on the competitive environment facing both shippers and carriers, the discussion also touched on the importance of the Merchant Marine as an arm of defense. The rationale for most forms of subsidy to the maritime industry, including cargo preference, is national security. The U.S. merchant fleet would be tasked in wartime with both direct military support and continued support of the civilian economy. DOD recently completed a study to determine wartime logistics needs and the adequacy of the merchant marine to fulfill them. The findings were that sufficient container capacity exists for carriage of containerized military cargoes. However, there is a significant shortfall of capacity — breakbulk[2] and Ro/Ro[3] to carry unit equipment. DOD has launched two initiatives to ameliorate this problem: 1) purchasing older breakbulk and Ro/Ro vessels on the open market and putting them in the National Defense Reserve Fleet (NDRF); and 2) purchasing the flat racks and sea sheds needed for converting containerships to carry large equipment, such as tanks.

Some participants raised the point that, even if sufficient sealift capacity is achieved, there may not be an adequate pool of merchant seamen to crew NDRF ships. The average age of U.S. merchant seamen is in the 50's, and newer commercial vessels are being operated with smaller crew complements. In addition, the commercial sector has little need for large numbers of replacement crews, and this reduces the pool of U.S. seamen even further.

---

1. This states that all intra-OECD trades would be exempt from the provisions of the Code and opens portions of OECD-to-LDC trades to all OECD members.
2. Ships which carry general cargo in a large variety of sizes.
3. Ships which carry vehicles or trailers that are loaded and discharged by "rolling on and rolling off."

Another issue raised was the cost of defense features on merchant ships. Theoretically, DOD pays the full cost of these features. Several participants questioned whether this is in fact the case.

PANELISTS' PRESENTATIONS

Charles Angevine,"Current Initiatives and Responses to International Cargo Policies Such as the UNCTAD Liner Code and Bilaterals With Major Trading Partners"[4]

The topic of this workshop is "Cargo Policy." As you will see, I believe that those two words may mean different things to different people. As all of you are aware I am sure, the policy of this Administration has been to, as much as possible, let the market determine the carriage of our trade. We do not intend for this Government to intervene in the choice of carriers by exporters and importers, nor do we intend to permit foreign governments to determine the choice of carriers for our trade. Furthermore, we do not intend to permit state-controlled carriers to walk off with our trade with third countries, nor do we intend to permit foreign governments to prevent U.S. carriers from competing for their trade with other countries. I will give you a few examples of how that policy has worked out in recent times.

More than two years ago, the Government of the Philippines attempted to implement, unilaterally, the UNCTAD Liner Code's cargo-sharing scheme in our trade with the Philippines. The Federal Maritime Commission faced up to this problem, as did this Administration. Supporting each other, the Administration and the Commission were able, through the use of Section 19 of the Merchant Marine Act of 1920, to have the Philippine Government remove the regulation imposing UNCTAD Code-like cargo sharing in our trades. More recently you have seen that on November 9, the Administration commented in the Section 19 case currently brought to the Commission by a Norwegian carrier in the Argentina-to-U.S. Trade.

The executive branch has fully supported the Controlled Carrier Provisions now incorporated in the new Shipping Act of 1984. These protect our carriers and other carriers in our cross-trades from the cut-rate nonmarket based competition government-controlled carriers are so well positioned to provide.

Finally, this Administration supported the legislation which ultimately resulted in Section 13(b)(5) of the new Shipping Act of 1984. This protects the rights of U.S. carriers to operate as cross-traders between two foreign countries. You can expect this Administration to actively support its use when necessary to protect the access of U.S. carriers.

In this panel this morning, I have been asked to comment on our responses to the UNCTAD Liner Code.

The UNCTAD Code came into effect just over a year ago because Germany and the Netherlands became parties to the Code just over a year and one-half ago. Since that time no other developed countries have become parties to the Code, but there are indications now that several others, probably led by the United Kingdom, are likely to become parties to the Code in the near future.

Originally, the United States, traditionally mistrustful of cartels and of closed liner conferences and also sympathetic to the developing country victims of the closed-conference system, thought there might be merit in a code of conduct for liner conferences. Unfortunately, it quite soon became clear that the code being negotiated was a mistake. And so, we had to vote "no" on April 6, 1974. The Code reflected principles contrary to the American economic philosophy, particularly the role of competition. The U.S. Representative to the Plenipotentiary Conference explained that three issues were especially critical to our decision to vote "no," and I would like to read what he said ten and one-half years ago.

First, he said,

> The membership provisions encourage the continuation of closed conferences. In this regard, it is ironic that the closed conferences system, which was so bitterly attacked by the developing countries throughout most previous UNCTAD shipping meetings, is now sanctioned on an international scale by those same developing countries under the auspices of UNCTAD.

Second, he said,

> The cargo-sharing provisions will cartelize the transportation of trade. Such provisions subordinate trade to transport. They restrict the choice of shippers and may result in delay of shipments and consequent loss of trade.

Finally, he said,

> The provisions on freight rates freeze them for unduly long periods, which could strangle the liner industry. Rate rigidity will hurt shippers as much as carriers.

I might point out that, as we read it, that rate rigidity could last for 15 months, which I do not think is very realistic.

Our response to the Code is to continue to oppose it and to oppose attempts by trading partners, whether they are major or minor, to force the United States into Code-like arrangements.

---

4. Director, Office of Maritime and Land Transport, U.S. Department of State.

I think everybody recognizes that even though the Code has been in effect for over a year, its direct effects on U.S. interests have remained small and probably will continue to remain small. For those not aware of this reasoning, let me explain. As the United States is not a party, the Code will not apply in our bilateral trades. The other developed OECD nations are not going to apply the Code to trades with each other. Our bilateral liner trades, and the liner trades between other developed countries, account for the vast majority of liner-borne trade. The only possible direct effects on U.S. interests will be on opportunities for U.S. carriers in the liner cross-trades involving developing countries, parties to the Code. Even then the effect of the Code will be limited because the other developed maritime countries have formulated the "Brussels Package," which, if operated as described by package members, will keep 60 percent of their conference trades with Codist developing countries open to competition from U.S. conference members. Furthermore, the other developed maritime countries maintain that the Code and its 40/40/20 formula apply only to conference cargo and not to cargo carried outside the conference. Finally, there is some evidence that even the most enthusiastic developing country supporters of the Code will see to it that the competitiveness of their most vital exports and imports will not be shackled by the Code.

To insure that the effects of the UNCTAD Code remain small, we have held a series of discussions with the Consultative Shipping Group (CSG), 12 European shipping nations and Japan, in seven rounds of discussion since June 1982. An eighth round is scheduled for next month here in Washington and, as have the other rounds, will focus on one seemingly simple concept — that the 14 developed countries involved would keep their trades with other countries open to each other's carriers. Of course the difficulty here is that our trades are essentially already open to any carrier who files a tariff, whereas it is questionable how open are the trades between the CSG countries and third countries. Therefore, the most critical problem is the assurances we need from the CSG on open access to their trades with developing countries.

So it becomes apparent that when this Administration speaks of "cargo policy," the policy is that the carrier of our cargo should be chosen by the shippers of our cargo, and that U.S. carriers should enjoy the ability to compete freely for cargo in U.S. and foreign-to-foreign trades. I want to remind you that when the U.S. Government is the shipper, it continues to support the enforcement of our Government Cargo Preference Laws, P.R. 17, P.L. 664, and the 1904 Act. I would also point out that the 1904 Act mandates that 100 percent of military cargo moves on U.S. ships.

And I suggest to those for whom the words "cargo policy" mean reserving cargo to

the U.S.-flag [fleet], that our Government cargo-preference laws do this quite effectively for about one-third of the cargo carried on U.S. ships, as shown by the G.A.O. report of January 31, 1984.

I also suggest that for our commercial U.S. shippers, our cargo policy means that they can choose the carriage of their goods unfettered by U.S. Government regulations and, to a large extent, unfettered by regulations of foreign governments. And should foreign governments attempt to make their choice for them, U.S. shippers will find their Government receptive to their complaints. They should make their complaints known not only to the Administration but most assuredly to the Federal Maritime Commission, whose Section 19 procedures this Administration will support fully.

In summary, I believe that the bilateralism of liner trades, represented by the UNCTAD Liner Code, is a failed and outmoded policy. The future is represented by the round-the-world service inaugurated by United States Lines today, December 3, 1984. That service, with the 12 largest container ships ever built, will only succeed in a world unchained by the shipping bilateralism of the past.

Deborah Christie[5]

One rationale frequently advanced for Government intervention in the market place of seaborne trade is the need for U.S. flag shipping to meet national security requirements. A necessary first step to evaluating the effectiveness of any cargo policy in meeting this objective is a fairly precise definition of what national security requirements are and what types and amounts of shipping are needed to meet them. Since many of our military requirements arise in the defense of allies, we also need a policy decision on the extent to which we are willing to rely on allied shipping to meet requirements.

Wartime national security requirements can be divided into three components:

- deployment and support of military forces
- support of defense industry
- support of the civil economy

Last spring, DOD completed a study of the dry cargo sealift required to deploy and support U.S. forces in a worldwide war. As a result of that study, the Secretary of Defense has proposed that, as a matter of policy:

- sufficient shipping capacity should be under US control to meet those re-

---

5. Division Director for Projection Forces and Analytic Support, Office of the Secretary, U.S. Department of Defense.

quirements for which allied shipping is not available, and

- we should obtain assistance from our allies, whenever possible, to meet requirements in their geographic areas.

Under the global war scenario currently used in defense program development, this policy would require U.S. shipping capacity to move about 800,000 short tons of unit equipment and 1.7 million short tons of resupply and ammunition. When we compare these requirements to capabilities we see no shortfall in capacity to move resupply and ammunition. On the other hand, we do not have an adequate capacity to move unit equipment today, and the capacity of the U.S.-flag fleet to move such equipment is projected to decline as containerships replace breakbulk ships, barge carriers, and RO/RO vessels.

DOD has two programs underway to reduce this shortfall. First, we are putting ships that are leaving the U.S. flag fleet into our Ready Reserve Force. Second, we are buying flat racks and sea sheds to enable us to move unit equipment in containerships in wartime. These programs can be expanded sufficiently to eliminate the shortfall completely, and the cost of doing so can be compared to the cost of alternative cargo policies that would expand the capacity of the U.S. flag fleet.

Let me emphasize that the shortfall we have identified is in ships capable of carrying unit equipment. Cargo policies that would encourage, for example, a larger containership fleet or more dry bulk carriers can not be argued for, based on the need to deploy and support U.S. forces.

Studies are underway on the requirements (1) for tankers to move bulk POL for the deployment and support of military forces and (2) for ships of all kinds to support defense industry and the general economy. Once these are finished, we will have a complete picture of national security requirements and be in a better position to judge the value of various cargo policies in meeting them.

Robert A. Ellsworth[6]

I have been asked to present a few remarks about the Federal Maritime Commission's (FMC's) role in shaping international trade policy. This is a task I accept with great enthusiasm, for I believe that recent events are moving the FMC in the direction of becoming a protector of U.S. interests and rights in liner shipping and away from

---

6. Director, Office of Policy Planning and International Affairs, Federal Maritime Commission.

the role of the traditional regulatory agency.

I use the phrase "traditional regulatory agency" with caution, because while that may have been the perception of the FMC, it never really had authority to commit what I call the twin evils of regulatory commissions, namely, to control entry or exit from the regulated industry or to interfere with commercial rate-setting practices. Certainly, the Shipping Act of 1984 continues that tradition and, in fact, removes what little authority we ever had over rate levels in the foreign trades under section 18(b)(5) of the Shipping Act of 1916. The only remaining vestiges of authority retained in the area of rate levels is the controlled-carrier sections of the new Act, which I believe is necessary because this category of shipping companies choose to play by a different set of rules.

I would like to sketch out for you the role I see evolving for the FMC in the area of international liner shipping. I believe that, surprising as it may seem, the FMC has been in the forefront of the recent "discovery" of the services component of our international trade sector. The service sector now accounts for over 69 percent of our output and 74 percent of our employment and while not as large in our foreign sector, the United States is the world's largest exporter of services, with 20-percent share of the world market. The continued growth in the services component of our international trade sector is predictable, given our apparent comparative advantage in areas such as information services, computer software, insurance, finance, and engineering.

As the service sector grows in importance, the Government, late as usual, has also begun to give it increasing attention in various trade forums such as GATT and the OECD. Ironically, one reason that the trade in services has expanded rapidly is that it was not subject to as many restrictions as the trade in goods, but there is an alarming trend towards governmental controls. It can only be hoped that governments will realize the irrefutable truth that open markets and free trade will produce more benefits to the world community than will attempts to overregulate and control the trade in services.

As the Government attempts to develop policies in the international trade in services, I think it instructive to see where we have gone in terms of one of the oldest services — shipping.

There are three basic provisions in the shipping statutes that serve to protect American shipping interests in the foreign trades. They are, in chronological order, section 19 of the Merchant Marine Act of 1920, the Shipping Act of 1978 (also known as the Controlled Carrier Act), and section 13(b)(5) of the Shipping Act of 1984. I would like to concentrate may remarks on recent section 19 actions at the Commission and

then discuss the FMC's new authority in the foreign-to-foreign trades, section 13(b)(5). Let me begin with our recent experience under section 19.

In the fall of 1982, two U.S. shipping lines filed petitions with the FMC citing discriminatory practices by the Government of Venezuela, which allegedly was denying them access to substantial amounts of U.S. exports to Venezuela. The Commission instituted a section 19 proceeding and on December 8, 1982, issued proposed rules that would have resulted in the suspension of the tariffs of the Venezuelan carriers serving the affected trades as of January 15, 1983. The implementation of these sanctions was negated by a Memorandum of Understanding between the U.S. Government and the Venezuelan Government, which was signed on January 14, 1983.

While the U.S.-flag operators' difficulties were resolved, at least on an interim basis, a third-flag operator (Concorde/Nopal) alleged that because of an increase in scope of the Venezuelan Law it was being denied access to cargo, and so in July 1983 it filed a section 19 petition with the Commission. A Memorandum of Consultation signed by the respective governments on September 9, 1983, once again averted the need for the FMC to impose sanctions.

Thus, while the FMC never had to impose sanctions against Venezuela, it is clear that the existence of this threat convinced the Venezuelans that the United States was serious in its intent to keep our trades as open as possible to competition. This was the first clear instance of the policymaking branch of the Government — the Administration as represented by various agencies, including Transportation and State — and the enforcement arm, the FMC, cooperating to ensure that our nation's shipping policy be carried out.

The Administration's policy towards cargo sharing in general and the UNCTAD Code in particular is that we will resist cargo sharing, but this resistance will be tempered by realism. In short, our policy towards nonmarket cargo-allocation schemes is to resist them to the maximum extent economically and politically possible.

In the ensuing months after our Venezuelan difficulties, two other section 19 petitions were filed with the Commission, one involving our trade with Ecuador, where a U.S.-flag operator alleged discriminatory treatment in its access to facilities, and the second begun by the Commission, on its own motion, when it instituted a proceeding in the Philippines trades. While both cases were important, I would like to focus on the Philippines because it presents a nice lead in for my next two topics, the UNCTAD Code and the U.S.-CSG discussions.

On January 19, 1982, the President of the Philippines signed Executive Order No. 769 (E.O. 769). E.O. 769 was a complex document, but the idea was to impose a 40-40-20 cargo-sharing regime in the Philippines trades. On July 22, 1982, the Philippine Government put into effect Memorandum Order No. 3 (M.O. 3), which implemented E.O. 769 in the U.S. trades, even though the United States had repeatedly stated that it was opposed to cargo sharing.

Almost from the inception, FMC began to receive complaints from shippers and third-flag carriers about the burden that E.O. 769 was placing on their operations. In September of 1983 the Commission, on its own motion, instituted a section 19 proceeding to determine whether E.O. 769 was creating conditions unfavorable to shipping in U.S. trades. The Commission received input from numerous sources, including U.S.-flag operators, Philippine carriers, shippers, and third-flag carriers. A concern for fairness led to the Commission permitting an additional round of reply comments. In this last round, the U.S. Government (i.e., the Departments of Transportation and State, and other agencies) submitted comments wherein they stated that there was little likelihood that bilateral discussions with the Philippines would be fruitful and, therefore, there was no recourse but for the FMC to impose the sanctions enunciated in the section 19 rule — that is, to suspend the tariffs of the Philippine-flag operators serving the U.S. trades.

Such a drastic step may not be necessary, however, because the Commission received notification on June 1, 1984, from the attorneys representing the Philippine carriers that the Philippine Government had withdrawn M.O. 3. For the time being, the United States has apparently been successful in its attempt to resist cargo allocation in an important trade.

Resistance to cargo sharing forms the backbone of the U.S. Government's refusal to sign the UNCTAD Code and the 40-40-20 cargo-sharing implications therein. The United States has repeatedly expressed its disdain for the Code and has consistently maintained its position since the Code's inception. The position is predicated on a shared belief that artificial cargo allocations create inefficient regimes and relegate our international trade in goods to a secondary position to shipping.

Despite U.S. opposition, of course, the Code is now a *fait accompli*. Ratification by West Germany and the Netherlands in April 1983 brought the Code into force in October 1983. The United States must now formulate policies to deal with this reality.

In an attempt to minimize the damage done by the UNCTAD Code, the U.S. Government has held a series of meetings with the Consultative Shipping Group (CSG),

which is comprised of European nations and Japan. The purpose of these meetings has been to develop mutual commitments to ensure that U.S. carriers are not locked out of CSG-LDC Codist trades and to meet CSG fears that the United States will enter into restrictive bilateral agreements.

Needless to say, these discussions are complex and by their very nature protracted, but the ultimate goal is so important that the time and effort are well spent. The most tangible results to date that demonstrate the sincerity of both sides have been the resistance to the Philippine cargo-sharing plan on the U.S. side and the development of the so-called "roundtable document" on the CSG side. The roundtable document was presented to the United States at our May meetings in Washington, and according to the CSG represents a "reservation" to the UNCTAD Code. In essence this reservation puts forth the position that the rights of nonconference lines are protected under the Code, but should a CSG Codist trading partner attempt to prevent nonconference lines from engaging in fair competition on a commercial basis then CSG nations may take appropriate steps to have the practice terminated. While the U.S. side wished this reservation could have gone further, it clearly is a positive step.

As part of the U.S. Government's efforts to keep the world trading lanes open to as much competition as possible, the Congress included a provision in the Shipping Act of 1984 which gives the FMC clear authority to protect the rights of U.S. vessel operators in the cross trades. Section 13(b)(5) was incorporated into the new law as an expression of the U.S. reaction to the UNCTAD Code. The concern was that as the Code came into force there would be a natural tendency to squeeze out U.S. cross-traders. Ironically, while U.S. shipping companies have not historically been known as cross-traders, many of our larger shipping lines plan to become more active in foreign-to-foreign trades just as the Code comes into force. Just how important this new provision will be is difficult to forecast, but if recent experience is any indication, then it is predictable that section 13(b)(5) will become an important weapon in our arsenal to keep liner shipping trades open.

The message contained in recent FMC section 19 proceedings, U.S. Government bilateral discussions with Venezuela, the Philippines and Japan, our discussions with the CSG and the advent of section 13(b)(5) of the new Shipping Act should be clear to all: the U.S. Government intends to resist cargo sharing, and it is going to maintain U.S. rights and interests in both our bilateral and foreign-to-foreign trades.

C. William Johnson[7]

Mr. Chairman: I am Bill Johnson, an international economist in the Office of Service Industries of the Department of Commerce's International Trade Administration. My responsibilities include the development of international ocean shipping policy for that Department.

The Department has an overall responsibility to promote international trade, especially American exports, plus a responsibility to promote U.S. service industries, including ocean shipping. There is a close link between international trade and ocean transportation. About 60 percent of U.S. international trade by value, and 99 percent of our international trade outside North America when measured by weight, moves by ocean vessel.

Ocean shipping is not an end in itself but is an essential service industry providing the link between manufacturers and their customers abroad. In the current conditions for world trade, with the strong dollar, the debt problems of a number of countries, and the strong recovery of the U.S. economy *vis a vis* the slower recovery in many parts of the world, American exporters are finding it difficult to compete abroad. Ocean carriers are seeing the results of this challenge as vessels, especially those in the Pacific trades, are virtually full inbound but have excess capacity outbound. The preponderance of our foreign trade is also shifting from our traditional trading partners across the Atlantic to new markets and suppliers in the Pacific basin. American producers are concerned that their task of competing abroad not be made more difficult by increases in regulations affecting the transportation of their goods or Government interference with how and with whom their goods are shipped. Our exporters want to be free to compete in markets abroad.

The most important issue in international ocean shipping today is cargo allocation, manifested by the entry into force in October 1983 of the United Nations Code of Conduct for Liner Conferences (UNCTAD Liner Code), with its cargo-allocation scheme, and the demands by some developing countries that the United States implement cargo allocation in our bilateral trades with them.

The United States voted against the Code in 1974 and has remained firmly opposed since. The United States is engaged in both bilateral and multilateral negotiations concerning cargo allocation.

---

7. International Economist, Office of Service Industries, International Trade Administration, U.S. Department of Commerce.

The current set of U.S.-CSG (Consultative Shipping Group — the European Economic Community [EEC], Norway, Sweden, and Japan) talks has as its principal impetus the U.S.-CSG split over the ratification of the UNCTAD Liner Code. The EEC, through adoption of the compromise Brussels Package reservations in 1978 provides the basis for EEC ratification. To date only two EEC countries, the Federal Republic of Germany and Netherlands, have acceded to the Code. Fifty-eight developing countries are party to the Code. The United States perceives the threat that U.S. carriers could be effectively shut out of European-LDC cross trades by: (1) LDC action to eliminate independent carriers; (2) closed-conference practices in European trades; or (3) a combination of both. We are also concerned about the precedent of the allocation of commercial cargo and its potential effect on U.S. exports and imports.

The U.S. objective is to secure guarantees for U.S. carriers of effective access to CSG-LDC trades. The CSG aim is continued access to U.S.-LDC trade equal to that which they currently have. Such an arrangement would be beneficial to both U.S. carriers and shippers. As American-flag carriers begin around-the-world service, it would assure the access to compete for cargoes in third-country trades that will be essential to maintain this service. The arrangement would also be beneficial to U.S. exporters and importers, since it would assure additional service for the carriage of their goods.

In our talks the U.S. Government and the CSG are moving closer to agreement on joint resistance to the unilateral implementation of cargo allocation and to making the commitments to keep our liner trades with third countries open to each other's vessels. We hope the CSG countries can make the commitments necessary to assure U.S. carriers access to their trades, as the United States is willing to do for CSG carriers.

The United States is also engaged in bilateral shipping talks with several countries. In these talks we are seeking to assure U.S. carriers access to the trades and the rights of American shippers to use the carrier of their choice.

Some shippers feel that anticompetitive elements of the Code and possible bilateral agreements, especially ones containing cargo-sharing provisions, and the potentially limited role of independent carriers envisioned by some developing countries, would inevitably lead to a deterioration in liner transportation service. These fears are based in part on experience with the pooling and/or equal-access agreements existing in some U.S.-Latin American trades, and on statements by officials of some developing countries, as well as on an understanding of the theory and history of cartel operations.

Potential impact on trade and shippers falls into two categories--rates and quality of service. The freight rate argument assumes that rates will increase at a faster than normal pace in the absence of competition in the shipping industry. This would increase the delivered price of foreign trade commodities and decrease their competitiveness in foreign markets. Not all products would be affected equally. Individual shippers whose products are more price sensitive than average, or for whom shipping costs are a particularly large share of total cost, would of course suffer disproportionately. For these products, greater percentage rate increases would lead to larger export sales declines. It is possible that modal substitution (e.g., utilization of tramp shipping) might mitigate the impact somewhat.

Shippers also fear a loss of sales and increased costs due to declines in the quality of liner service. Nonmarket determination of liner market shares would allow carriers to alter their schedules and port range in order to increase vessel utilization rates and profits per ton. To shippers this can mean less frequent sailing, especially between smaller ports; an increased probability of a shipment being left in port because of insufficient capacity availability; and a general decline in the reliability of service. Although these impacts are difficult to quantify, their costs to shippers are very real.

U.S. policy is to promote free trade. It is also important for the United States to improve its export performance and keep the costs of its imports down. Therefore, it is essential to have efficient, low-cost shipping services for American exporters and importers. This efficiency can be best maintained in a market that fosters competition in service and rates along with innovation to improve service and reduce costs. This can be best accomplished in a competitive market, basically free of cargo allocation.

Kay L. McLennan[8]

Good morning and thank you for the opportunity to share some thoughts on P.L. 664 (commonly referred to as the "Cargo Preference Act of 1954") and its influence on U.S. policies to promote agricultural exports. The Office of Transportation has studied the cargo-preference issues impacting U.S. agriculture and this work will form the basis of my comments on the cargo-preference mandate applicable to farm exports. After presenting a brief overview of the cargo-preference statute, I will discuss the impact of the Cargo Preference Act on agricultural export-promotion activities and conclude by highlighting the various cargo-reservation topics that have been identified as needing further analysis.

Cargo preference is the specific type of cargo-reservation policy which requires that a percentage of the cargo that is owned or concessionally financed by the U.S. Government to be carried on U.S.-flag ships. There are three statutes — the Military Transportation Act of 1904, Public Resolution 17 of the 73rd Congress, and P.L. 664 — which require U.S.-flag vessels to be utilized in transporting Government-impelled cargoes. The specific Government-impelled cargoes subject to the first two cargo-preference statutes include all military cargoes and all shipments financed by the Export-Import Bank, except that 50 percent may be waived to ships of the recipient country. The third statute, P.L. 664, requires that 50 percent of U.S. Government foreign assistance shipments, such as the Department of Agriculture's (USDA's) Food for Peace or P.L. 480 programs, be moved on privately owned U.S.-flag commercial vessels.

The Provisions of P.L. 480. — The United States has historically been the world's leading food donor. In 1954, major U.S. agricultural commodity aid programs were authorized through enactment of Public Law 480. The objectives of this law were to facilitate the disposal of large U.S. food surpluses, to assist countries that lacked sufficient foreign exchange for commercial purchases, to continue U.S. support of foreign aid efforts in Europe and other areas, and to develop U.S. commercial markets. The goals of the food aid program have increasingly emphasized the promotion of economic development and the reduction of hunger and malnutrition abroad.

The two major programs under P.L. 480 that are subject to the cargo-preference mandate are Title I (Concessional Sales) and Title II (Donations).

Under Title I the Government, through the Department of Agriculture's Commodity Credit Corporation (CCC), finances the sale and export of commodities, with the actual sales being made by private U.S. suppliers to foreign importers or government agencies. Since Title I is a credit program, the U.S. Government is not party to the sales contracts but does oversee the transactions by reviewing each contract regarding price and conformance with purchase authorization requirements.

The recipient country, in addition to arranging for the procurement of the commodities, also arranges for the ocean transportation of Title I sales. USDA pays a portion of the freight cost — the ocean freight differential. This differential is any extra freight cost that may be incurred when 50 percent of the commodities shipped are carried on U.S.-flag vessels in accordance with P.L. 664, the Cargo Preference Act. In addition, USDA is responsible for assuring that at least 50 percent of Title I cargoes are

---

8. Economist, Office of Transportation, U.S. Department of Agriculture.

shipped on U.S.-flag vessels.

Title II donations encompass all grants of agricultural commodities under the P.L. 480 exports which are distributed by cooperating sponsors. The Agricultural Stabilization and Conservation Service (ASCS) of USDA provides all commodities shipped under Title II, either from CCC stocks or through purchases from commercial markets. The ASCS maintains shipment information and the CCC pays the full ocean transportation costs. The Agency for International Development generally handles oversight for the ocean transportation of Title II cargoes and insures that cargo preference requirements are met.

Economic Costs of Cargo Preference Compliance. — Compliance with cargo-preference laws — shipping at least 50 percent of our P.L. 480 cargoes on U.S.-flag vessels — represents additional program costs for Title I and Title II exports. Specifically, USDA paid $120 million in Title I ocean freight differential costs in 1982. This amount represents slightly over 14 percent of the total program costs for this year. Although separate differential payments are not made in the Title II program for the same country, the difference between U.S. and foreign-flag charters can be as high as in the Title I program.

The cumulative costs of our P.L. 480 programs totaled $11.5 billion as of 1982. The ocean freight differential payments were $830 million, or 7.2 percent of the cumulative total costs. Further, a cost related to cargo-preference compliance arises when cargoes are in a large enough parcel size to warrant chartering a vessel, but are broken apart into smaller parcel sizes and shipped on liner vessels to assure compliance with U.S.-flag preference requirements.

Finally, according to the data compiled for the Office of Transportation by a private consultant's group, the derivative or nontransport costs, although a part of cargo-preference compliance, are not typically considered since they are not readily measurable. The derivative costs include private and public administrative costs, land transport, and special facilitation differential costs, and any market or program effectiveness losses.

Does Cargo Preference Impede Export Promotion? — To begin with, although I have been asked to address the issue of the impact of cargo-preference compliance, I want to stress that USDA recognizes the President's commitment to the existing cargo-preference laws. The Administration's point of view was reiterated by Admiral Shear, Maritime Administration of the Department of Transportation, when he appeared before

the Subcommittee on Merchant Marine of the House Merchant Marine and Fisheries Committee to discuss the Government-Impelled Cargo Act (a bill introduced during the 98th Congress). More specifically, Admiral Shear stated that:

> The Administration continues to support these laws (that is, the cargo-preference laws currently in effect), and where required, would support an appropriate clarification of existing law. However, we do not support either an expansion or a contraction of the scope of current law.

Arnold Levine[9]

Thank you. Going last gives me the opportunity to pick and choose so as not to cover the territory covered by previous Government speakers. Let me briefly review several elements of our international maritime cargo policy, starting with what I will call the competitive environment and how one characterizes that.

It is characterized I think by a commitment to maintaining open trades, to maintaining open conferences, and to encouraging or making mandatory the right of independent action in conference proceedings. That competitive environment and the policies that shape it are basically flag-blind, as has been indicated earlier, the principal exceptions being government-controlled carriers' access to the U.S. market (i.e., those subject to the Controlled Carrier Act) and our own cargo-preference requirements. Overall, we seek to maximize the amount of cargo that remains fully competitive.

The second element of our international maritime policy deals with the extent of Government involvement in the maritime industry. With respect to the economic and operational aspects of the industry, the thrust is to reduce Government involvement. We are seeing the phaseout of direct subsidy programs. We are proposing that carriers be given greatly increased operating flexibility and that shippers be given a broader range of choice. Carriers are freed up to enter into inter-carrier agreements to an extent never seen before in the U.S. trades, and we are encouraging rate flexibility and innovation.

A third element which I think we would have to speak to is the area of preference cargo. As an overview, I would echo what we have heard as a statement from the Agriculture Department, that is, that it is the Administration's policy to support and continue the existing cargo-preference programs, and to oppose any expansion of those programs. In that context, there has been a suggestion that perhaps the current cargo-preference laws can be made to work better. The Administration is prepared to discuss any coverage- or scope-neutral proposal along these lines.

---

9. U.S. Department of Transportation.

At this point I will call on Lewis Paine from the Maritime Administration's Office of Market Development to discuss preference cargoes. After his remarks I will speak a bit about international maritime relations with our trading partners.

Lewis C. Paine[10]

Thank you. My remarks this morning will address the effectiveness of cargo preference as we know it today.

The three existing cargo preference laws which apply to U.S.-Government-generated ocean-borne cargoes moving on foreign trade routes reflect a consistent policy of our Government. The origin of this policy can be traced back to the very first year of our nation's existence, when initial legislation was enacted to reserve specific cargoes for the merchant marine.

The world shipping environment today is influenced by numerous countries which have some type of cargo-preference law. Too frequently these extend beyond government-sponsored cargoes to cover cargoes in the commercial trade of the nation as well. The record is clear that our cargo-preference laws are the most flexible, commercially attuned, and liberal in operation in providing access by vessels of other nations to these cargoes, except for the Department of Defense's own troop support shipping requirements.

There exists a concern that U.S.-flag carriers are more expensive than foreign-flag carriers, and therefore, that the cargo-preference laws encourage inefficient operations and unnecessarily restrict the flow of our exports. The application of the cargo-preference laws to most civilian Federal programs and cargoes has resulted in no additional freight differential cost being incurred by the agencies. Where differentials have resulted, the actual differential amount, with few exceptions, was less than 1 or 2 percent of the agency's total ocean freight bill for the year. Exceptions to this are the P.L. 480 Title I program and the Strategic Petroleum Reserve, both of which generate high volumes of full cargoes, requiring bulk vessels.

U.S.-flag liner operators have been essentially competitive with foreign-flag liner rates. They are further increasing their competitive capability with larger container vessels, carefuly integrated intermodal systems, reduced manning scales, and fuel-saving propulsion machinery. Freight differentials on liner movements are of a minor nature.

---

10. Acting Associate Administrator for Marketing and Domestic Enterprise, Maritime Administration, U.S. Department of Transportation.

It is true that, for some program participants on some preference cargoes, significant differentials in freight costs have existed between U.S.-flag and foreign-flag bulk vessels. However, over the past 4 years, there has been a very substantial reduction in the cost of shipping agricultural commodities under U.S. foreign assistance. This has been achieved through the introduction of large, modern, efficient U.S.-flag carriers in our bulk trades. These modern vessels are the result of government maritime programs and of the initiative and determination of American ship owners.

In the area of maritime labor, there have been appreciable advances in the reduction of crew costs and the acceptance of competitive manning scales. Thanks to the understanding and foresight of labor leadership, that progress is continuing.

Egypt is the largest recipient of cargo under the P.L. 480 program and illustrates well our achievements in providing more efficient vessels and lower freight rates for the bulk trade. Over these last 4 years, through the chartering of these larger, more efficient vessels, on average the U.S.-flag rates on bulk grain shipments to Egypt were reduced by 52 percent. These reductions were directly applied to reducing the ocean freight differentials to the United States Department of Agriculture and the Agency for International Development. It is also noteworthy that these accomplishments have been achieved with a dedicated joint effort by USDA and AID, the vessel owners, the Maritime Administration and the recipient country in facilitating utilization of larger vessels carrying larger cargoes.

Four years ago the extent to which old ships were used to transport these Government-impelled cargoes was of great concern to all Federal agencies involved, as well as the Congress and the recipient countries. We have made major progress in eliminating aged bulk vessels. During the past 2 years foreign scrappings have been approved by Admiral Shear, the Maritime Administrator, which have or soon will rid the U.S. fleet of more than 60 old rustbuckets. Further scrappings will be encouraged.

In calendar year 1981, 61 percent of all the full cargoes of bulk grains to Egypt which moved in U.S.-flag vessels were transported in vessels exceeding 22 years of age. Only 21 percent were transported in vessels aged 5 years or less. In 1984 to date, 63 percent of these grains were transported in vessels aged 5 years or less, and the oldest vessel to participate was only 12 years old.

Incidentally, I think it should be noted that the foreign freight differential cost has a substantial relationship to the very low rates provided by foreign-flag bulk carriers. These rates are due to the persistent and disastrous overtonnaging in the world market. In many instances, the foreign operators are not covering a penny of their capital costs

or depreciation. When that market returns to normal, any ocean freight differential will decline sharply.

And, incidentally, it's interesting to note that while in 1982 the ocean freight differential for USDA Title I was $120 million, in 1960 it was $64 million. In 1983 it was $65 million. The average for the past 16 years has been $62 million per year.

The revenue impact on the U.S. Merchant Marine from civilian agency programs in 1982 was in excess of $635 million. The Department of Defense's troop support cargoes generated U.S.-flag revenue in excess of $1 billion. Any encroachment or derogation of these laws or their application to the federally sponsored cargoes will therefore seriously jeopardize the U.S.-flag shipping industry without any significant net benefit to the U.S. Government.

It must also be recognized that use of U.S.-flag vessels is as much an export of the United States as that of any other commodity involved in these programs. Similar multiplier benefits come into play for the U.S. economy when these vessels are used. Our balance of payments is significantly enhanced through the use of U.S.-flag vessels.

The cargo-preference laws also favorably benefit every segment of the merchant marine. The cargoes carried by U.S.-flag vessels as a result of these laws enable the liner carriers, for example, to have base cargoes to build upon and compete for the commercial cargoes and normally marginal or unprofitable trades to the less developed countries. The capturing of the commercial cargoes in these situations further enhances our serious balance-of-payments situation.

To assure total compliance with any law is a challenge in this age. Nevertheless, dialogue between the Maritime Administration and the various Government shipper agencies, as well as private sector contractors subject to these laws, has escalated dramatically in recent years. This has resulted in an increasing understanding of the requirements of the cargo preference laws by shipping organizations and shipper organizations.

The new Federal acquisition regulations that became effective only last April provide far more specific directions as to these requirements than did previous regulations. As a consequence of these activities, compliance with the laws has broadened substantially. This trend will continue.

It is our view that no new legislation *per se*, nor expansion of the current cargo preference laws relating to government-impelled cargo, is necessary or warranted. Support and compliance by the Federal agencies with the existing laws would provide the

essential opportunity embodied in these laws for the Merchant Marine and the Federal cargo environment. Thank you.

Arnold Levine (continued)

About one-third of U.S.-flag carriage is comprised of preference cargoes, which clearly underlines the importance of these programs to the U.S.-flag fleet. On the other hand, it is a small enough portion of our total trade that the effect of the U.S. cargo-preference programs on the competitive environment is such that our trading partners have an excellent opportunity to compete in U.S. trades. Preference cargoes account for just 4 to 8 percent of our total liner operations. What we see, therefore, is a multiplying effect on U.S.-flag vessels from those programs. At the same time, the effect of the programs does not distort the nature of our liner trades.

Along that line, let me wrap up my comments by speaking a bit about our relations with our international maritime trading partners. As is the case in many areas of economic activity, we stand apart from the rest of the world in many respects. We have, when our policies differ from those of our trading partners, a number of options to pursue. One would simply be to try to convince our trading partners that we are right and they should adopt the U.S. approach. In the maritime area that hasn't proven too terribly effective.

A second option would be simply to adopt our partners' approach — and there I am thinking in particular of the UNCTAD Code of Conduct for Liner Conferences. We have said no, we will not.

A third approach would be to oppose vigorously those contrary positions. There again, although we have taken a policy of opposing the UNCTAD Liner Code, we have not set out to oppose all policies by other countries that may in some degree conflict with ours.

The final option, and one where I think we are working now, is that we accept some proposals by other countries, oppose others flat out, and compromise on any number of others.

I would like to give you a quick list of what I think we are trying to achieve at this point in our relations with our maritime trading partners. First of all, the Administration is committed to defend the rights of U.S.-flag carriers as direct traders in our bilateral trades, and we do this principally through the use of section 19. To protect carriers' rights as cross-traders, we now have a very potent instrument in the form of section

13(b)(5) of the Shipping Act of 1984. These defenses would be accompanied by discussions and negotiations with our trading partners as a means of resolving our differences.

I think an important element of these relations is that [certain of these protections are available to foreign-flag carriers] on a flag-blind basis — that is, in the case of section 19 remedies, they are available to foreign-flag carriers in U.S. trades who believe their access is being impaired, and they are available to shippers in the U.S. trades who believe that their freedom of choice is being infringed.

We also recognize the legitimate promotional interests of developing countries. We have not in effect told the trading partners with whom we have engaged in bilateral discussions to this point (for example, Venezuela, the Philippines, and Malaysia) that under no circumstances will we tolerate any cargo sharing, nor any promotional schemes in those trades. Instead, we have basically looked at our system and said, we [are willing to discuss with you an arrangement that closely] mirrors [the promotional activities that we ourselves are following] in our trades. It is on this basis that we have tried to deal with the developing countries, essentially offering to recognize legitimate promotional interests [relating to the development of their] maritime industries. There is, however, a point at which these promotional interests cease to be legitimate — that is, where the tail of promotion starts wagging the dog of competitive trade. It is in that connection that we are resolutely opposed to the imposition, particularly the unilateral imposition, of stringent cargo-sharing bilateral arrangements.

Thank you.

PANEL ON INDUSTRY IMPACTS OF LINER CARGO POLICIES

December 3, 1984

PANELISTS

Peter Finnerty
Sea-Land Industries

Bonnie Green
American President Lines

Peter Luciano
Transportation Institute

Sam Nemirow
Council of American Flag Ship Operators

Robert Rickert
E. I duPont de Nemours and Company

Roger Wigen
3M Company

TOPICS FOR DISCUSSION

1. Impacts of current cargo-preference laws and regulations on the trade, on shippers, and on carriers — including estimates of costs and benefits now and in the future.
2. Impacts of current bilateral agreements; prospects for future bilaterals and their effects.
3. Experience to date with implementation of the new Shipping Act; prospects for benefits to shippers and carriers.
4. Experience to date with the UNCTAD Liner Code and prospects for future impacts on the industry.
5. Experience with changing international approaches to cargo policies and impacts of cargo policy initiatives of major trading partners.

SUMMARY OF DISCUSSION

Liner operators emphasized the importance of preference cargoes to their sector of the industry. While these cargoes may account for a small percentage of all liner cargoes, they frequently are "base cargoes" that allow operators to carry commercial cargoes on routes that otherwise would not be profitable. This is even more true for exports than imports, because on some routes (LDC trades in particular) AID cargoes may comprise the preponderance of all U.S. exports. At a time when commodities are hard to sell abroad due to the strength of the dollar, Government-impelled shipments are particularly vital to carriers. Liner representatives also pointed out that there is very little disparity in liner rates between U.S.- and foreign-flag conference carriers, since rates generally are set by a conference and adhered to by all conference members. However, a GAO study reported that U.S.-flag liner carriage under the P.L. 480 Title II program cost $0.73/per ton more than foreign-flag carriage in 1980 — an annual premium of $600,000.[11]

Implementation Issues

Liner operators are not pressing for expansion of cargo-preference laws. However, they are extremely concerned that current laws are not being adequately enforced and that U.S. carriers are not getting the share of cargoes they are due. Participants suggested that part of the problem is that MarAd does not receive information on cargo carriage until well after the movement; it is difficult to enforce compliance after the fact. Concern was greatest with respect to agricultural cargoes. In 1983, all agricultural programs subject to P.L. 480 had U.S.-flag shares below 50 percent. Liner operators claimed that many new programs, such as the "blended credit" program, are not subject to preference requirements at all.

In addition, a number of DOD programs are not covered. The new Federal acquisition regulations should help with this, but they call only for 50-percent preference, while the 1904 Act requires that 100 percent of DOD cargoes are to be carried by U.S.-flag ships. Carrier representatives also were concerned that the Military Sealift Command frequently contacts a carrier asking for berth-term availability, and then later enters into the charter market for the same tonnage. Some ExIm Bank programs, like the short and medium-term guarantee programs, do not have U.S.-flag requirements. Finally, conversion of AID's commodity-export program to a cash-transfer program effectively diminished U.S.-flag participation. Carriers asked for action to assure implementation and enforcement of preference laws, including a statement from the President ordering agencies to comply fully.

Shipper representatives expressed a different point of view on trade barriers generally, whether cargo-preference, conference action, or bilaterial or multilateral cargo reservation. All trade barriers are inefficient and uneconomic. An example was given of shipping a container from the Midwest to Argentina or Brazil: via Europe, the cost is $3,400, while direct shipment costs $5,000. Shippers were optimistic that the new Shipping Act addresses some of these problems. However, they still have some concerns. Conferences can set rates, pool revenues, restrict sailings and volume capacity, and prevent competition. Ultimately the success or failure of the Act will be depend upon how carriers respond to the independent action provision incorporated in the law. Shippers are also optimistic that the new Shipping Act will result in a better balance between

---

11. U.S. General Accounting Office, *Economic Effects of Cargo-Preference Laws*, GAO/OCE-84-3 (Washington, D.C.: GAO, Jan. 31, 1984).

carriers and shippers than existed under the 1916 Act. Competitive opportunities are available to both shippers and vessel owners, including the ability to provide intermodal services,[12] independent action,[13] and a prohibition against loyalty contracts,[14] except as allowed under antitrust law.

Thus far, the impact of the 1984 Shipping Act has varied by trade area. In general, carriers in the OECD trades have been more aggressive in implementing its provisions than have those in LDC trades. Independent action has become common in the Pacific trades, while carriers on the North Atlantic appear afraid of starting a new rate war. Individual shippers have taken advantage of new provisions such as service contracts to a greater or lesser degree. Shippers' associations are not yet common, and leaders in organizing them have yet to come forward. Many shippers fear antitrust problems and therefore have adopted a "wait and see" posture.

Access to Foreign Trades

The second major topic addressed by the panel was the difficulty faced by U.S. cross-traders in an increasingly protectionist international environment. The liner companies regard their cross-trading activities as very important financially, not only to themselves but to shippers. The ability to pick up cargoes as space is available means that carriers can improve utilization of available capacity, and thereby reduce rates. Again, the Shipping Act was mentioned as an important protection for cross-traders. Under section 13(b)(5), FMC may suspend U.S. tariffs of the flag carriers of any nation in U.S. trades which discriminates against U.S.-flag cross-traders in its trade with third country.

The final major issue raised by members of the liner panel was the lack of consistency in U.S. policy — that is, an indecisiveness as to whether the merchant fleet is a commercial entity or a Government entity. Most countries regard their merchant marine as an arm of government. The United States, on the other hand, seems to believe that its merchant fleet should compete commercially and yet should be readily available to support U.S. Government interests. At some point, U.S. policymakers must grapple with the problem that some parts of the industry may survive on a commercial basis, but they

---

12. A contract for shipping services covering several modes of transportation (truck, rail, ship, etc.).
13. The right of a carrier in a conference to offer independent service and rates.
14. Confidential loyalty agreements between shipper and carrier in exchange for favored rates.

may not be sufficient to support broader U.S. interests. DOD is embarking upon development of its own merchant support fleet, which may or may not be the most efficient way to serve the national interest. It was suggested that, before the United States is committed to letting the merchant fleet as it currently exists die and be replaced by a defense-oriented merchant fleet, the long-term costs and benefits should be weighed and a conscious policy developed.

PANELISTS' PRESENTATIONS

Peter Finnerty[15]

I would like to use my time today to speak to the issue of liner shipping cross-trading for U.S.-flag carriers. It is an issue that is often confused, and it is one that is increasingly important as we address the area of cargo allocations and bilateral policy both in the U.S. trades and in terms of the UNCTAD Code and CSG talks.

I might underscore that cross-trading by U.S.-flag liner carriers — and I stress the plural — is a very important part of their overall business. Sea-Land has for many years engaged in a very significant amount of cross trading between foreign countries on the vessels that are employed in the import and export of American liner cargoes. It has, as a consequence, been very helpful and supportive to the economics of U.S. commerce. Carriers other than Sea-Land are also — and have in some cases long been — very active cross-traders. Delta Line, for instance, was a very active round-South-America cross-trader; American President Lines, many years ago, operated an around-the-world service in a westbound direction; United States Lines and APL and others to this day engage in cross trading between important countries in their services overseas, both in the Far East and increasingly in other areas.

This I state because I think one of the misimpressions both on the part of our Government policymakers and, indeed, many people in the private sector, is that cross-trading opportunities for U.S.-flag carriers is for some reason not important to shippers. I am here to try and disabuse them of that notion.

American shippers in a sense benefit by the economics of U.S.-flag carrier cross-trading. If those carriers are precluded from filling their ships up between foreign ports with way cargoes, it will detract from the economic and financial circumstances that those companies now enjoy or now have earned. Over a period of time, this would increase the pressure on all of those lines to try to recoup their total costs and earn a decent profit solely on their U.S. imports and exports.

If American policy is to be thorough in its approach to the whole question of liner shipping policy, it must address U.S.-flag carrier opportunities to cross-trade between foreign countries, not only for the sake of those U.S.-flag carriers, but also to some extent on behalf of U.S. importers and exporters.

It is unnatural to do what usually happens, and that is to treat the U.S.-foreign commerce as though it is somehow unique and completely separate from cross-trading in the liner business. With container technology and the economies of load-center ports and feeder ships and, more currently the rage, round-the-world services, it is an integral part of the overall economics of the business. It must be treated as such by our policymakers in their negotiations with other countries.

Robert Rickert[16]

The topic I wish to discuss is experience to date with the implementation of the Shipping Act of 1984. I have chosen this topic because I feel the Act contains a policy theme that is most important to the purposes of this workshop. The theme is competition. The Act tells carriers to compete among themselves, and it tells shippers to get together with carriers and compete in foreign markets.

There is another policy statement in the Act. Section 18 says that we are not afraid of change, that we will measure the effectiveness of the Act for 5 years, and then will make an evaluation. This evaluation could indicate that a change in direction is needed, or perhaps just a few adjustments, or perhaps more of the same. But we are saying that if we have to change, we will.

Experience cannot be discussed without first looking at objectives. Throughout the legislative process the objective of shippers was to ensure that any maritime regulatory bill that was enacted had shipper-carrier balance, a factor that was not in the 1916 Act. Shipper involvement in the process brought other parties to the realization of shippers' needs. This shipper involvement also gave shippers the responsibility to stay involved.

I would now like to mention those provisions in the Act which not only represent shipper objectives but are also what I consider to be shipper-carrier competitive opportunities. Keep in mind that these opportunities must be viewed as a chance for shippers and carriers to enter a business relationship to the benefit of both, a win-win situation.

---

15. Sea-Land Corporation.
16. E. I. duPont de Nemours and Company.

These opportunities are: the ability of conferences to provide intermodal services; independent action; the prohibition against loyalty contracts except in conformity with the antitrust laws; time-volume rates; the ability of shippers and carriers to enter service contracts; and shippers' associations. The use of these opportunities should be the standards against which experience or, if you will, the impact of the Act should be measured.

Of course, with the Act in effect for only about 6 months, experience is quite limited and conclusions meaningless. The final immplementation rules have just been issued by the Federal Maritime Comission, so shippers and carriers are still groping and perhaps scheming. You must expect many more months of a gradual upturn in the learning curve. Remember the 1916 Act was in place for 68 years with habits, philosophies, and traditions well engrained.

So far the impact of the Act is a mixed bag and varies by trade area. Carriers in the competitive OECD routes tend to be more aggressive in their interface with the Act than carriers in the trades with developing countries. For example, other than the cancellation of dual-rate tariffs, there has not been any effect as yet in the South American trades. This is undoubtedly because of the strong cargo-reservation tendencies in those routes. The concern of shippers is whether or not the competitive aspects of the Act will ever make any penetration.

I guess that some time in the future there will be a confrontation between the cargo-reservation provisions in bilateral agreements and the competitive aspects of the 1984 Act. The Act reflects the competitive thrust wanted by shippers, and should not be frustrated by cargo-reservation agreements.

In other geographic areas the impact is varied, possibly because of economic conditions. The strong dollar, as you well know, makes exporting a difficult task. In their efforts to get outbound cargo, conferences are most cooperative with reasonable rate proposals, minimizing the need for independent action.

In the Pacific trades, carriers are using independent action to maneuver among their peers. On the other hand, the North Atlantic carriers tend to stay clear of independent action for fear of reigniting the rate war. All in all, shippers are grateful that independent action is there to use as an opportunity for both shippers and carriers.

As far as the other competitive opportunities go, we have seen conference activity on intermodal service and interest in quoting those time-volume rates. Since Dupont has always taken our loyalty contract commitments seriously, the loyalty contract prohibition has given us flexibility that we did not previously have.

Dupont does not intend to participate in any shippers' associations, at least in the near future, even in areas where our cargo volume is quite small. There is no question that the subject of shippers' associations, as covered in the Act, is a frontier that begs for a pioneer or two. Many shippers are waiting to see what happens, their caution rooted in antitrust concerns.

Dupont is in the process of negotiating several service contracts. It is interesting to note that FMC has over 200 [such contracts] on file with most of these covering inbound shipments from the Far East. Service contracts will take time to develop and will not be suitable for all shippers and carriers. In Dupont's case we have foreign subsidiaries to supply and a reliable low-cost liner service is critical to our overseas presence. Our service needs are many and we are willing to make a commitment with penalty clauses. Not every shipper has the same needs.

For any carrier that wishes to negotiate a service contract with us, my advice is to leave your tariff specialists and admiralty attorneys at home and bring a contract lawyer. We want a contract, not a glorified time-volume rate or a mutated loyalty contract. Some carriers with whom we are negotiating grasp the concept well, others not as readily; but they are trying and they are learning. We are learning as well. The next time around will be easier, and the time after that easier still.

My comments on experience with the Act would be incomplete without a few words on reaction to the Act by the various people involved. In my opinion, FMC has been most positive and accommodating in their approach to the implementation rules. Their willingness to listen to shippers, carriers, and other interested parties, and accept advice, has made implementation much easier for us all.

As for shippers and carriers, the overwhelming majority are bullish on the Act. Naturally there are some that feel the other side got too much or the Act did not go far enough — but these are but a few.

As for benefits, they are there if you want to use the opportunities presented. As with most things in life, shippers and carriers are going to get out of the Act as much as they want to participate in the opportunities.

As I mentioned earlier, the opportunities must be viewed as a chance for shippers and carriers to enter a business relationship to the benefit of both. Each must realize that there has to be a gain for the other, a win-win situation. However, if shippers and carriers do not take advantage of the Act, there cannot be any benefits: nothing in, nothing out.

Hopefully, this time next year, with 18 months of experience, we will see things more clearly. To date things do look good and upbeat.

Bonnie Green[17]

Thank you. I am glad to be here today on behalf of American President Lines (APL). My focus is going to be the current cargo-preference laws and the way they affect the U.S.-flag liner trade.

Since the cargo-preference laws were reviewed in the earlier panel, I just want to go over them very briefly: the 1904 Act, which is the 100-percent U.S.-flag requirement on DOD cargoes; Public Resolution 17, which addresses the Ex-Im Bank program; and P.L. 664, which covers civilian agency shipments. Looking at the cargo-preference laws, these statutes affect only Government-impelled cargoes, that is, shipments that would not occur without Government involvement.

In adopting cargo-preference legislation, a major aspect of our foreign aid is benefit to producers through disposal of surplus domestic productions. This benefit is extended to the U.S.-flag carriers as a U.S. service industry.

The cargo-preference laws provide an entitlement to what have become base cargoes for liner carriers on certain trade routes, enabling liner operators to compete for commercial cargoes in the process of a profitable voyage. U.S.-flag liner operators essentially are competitive with foreign-flag rates. Lew Paine addressed the issue of the more modern container vessels and reduced manning scales this morning. Generally in the liner trades we are not talking about an ocean freight differential between U.S.- and foreign-flag operators.

In the area of cargo preference, the most difficult problem facing U.S.-flag carriers is access to those cargoes supposedly covered by the current cargo-preference laws but not available to the U.S.-flag companies.

The Maritime Administration (MarAd), as the agency monitoring compliance, does not receive information on most cargo-preference shipments until substantially after the shipment has taken place. If the agency or contractor has not complied with cargo preference, the cargo opportunity has been lost forever by the industry. Delayed reporting makes it difficult to know whether agencies are in fact complying with the cargo-preference laws. Since there are no penalties for agencies that do not comply, there may be only a limited effort by the agency to meet the requirement.

Specific areas of concern in the liner trades are agricultural programs. For example, in 1983 all of the agriculture programs subject to cargo preference, that is, P.L. 480 Title I and Title II and the section 416 dairy program, were below the required 50 percent. Since U.S.-flag service was available, there is some question, at least in the minds at APL, as to why the agencies did not meet this requirement.

Other USDA programs, such as the GSM102 program (a concessionary sales), are specifically exempt from cargo preference. New programs, such as the blended credit, are designed in such a way as to be outside of the cargo-preference framework.

Major DOD programs, such as the F-16, the F-18, and Navy vessel procurement that involves substantial foreign procurement, are outside of the cargo-preference framework. These commodities enter the U.S. duty-free because they are all for DOD, and yet there has been no cargo-preference requirement in the many subcontracts in the hundreds of millions of dollars.

The new Federal acquisition regulation is to address this shortcoming, but in many cases will only include a 50-percent requirement. We are also talking about thousands of contracts which are certainly beyond the scope of MarAd to follow, so it becomes a requirement of the U.S.-flag carriers to go out and find the contracts, find the cargo, and then go back to MarAd for assistance in ensuring compliance.

So while on its face it appears that the 1904 Act is a 100-percent requirement on DOD cargoes, this is often not the case. In addition, some DOD agencies take the position that if title has not passed to DOD at time of shipment, again it is only a 50-percent U.S.-flag requirement.

A key issue facing U.S.-flag carriers in the area of DOD cargoes is the competition that we are facing between berth-term operations and charter operations. It is not unusual to be approached by the Military Sealift Command (MSC) regarding berth-term availability for a substantial amount of cargo, only to have MSC enter the charter market for the same tonnage. We are then in a position of having to offer on a charter basis or losing that opportunity. This raises some questions as to whether DOD is really treating the U.S.-flag liner carriers offering berth-term rates in the way intended under the 1954 Act and under the Wilson-Weeks agreement.

New Ex-Im Bank programs, such as the short- and medium-term guarantee program, do not include a U.S.-flag requirement. While the Bank has a financial risk and

---

17. American President Lines.

in many cases has had to pay out on loans that have not been honored, the Bank maintains that there is no U.S.-flag requirement. MarAd has taken a position that these programs should be subject to a U.S.-flag requirement, but it has been unable to come to an understanding with the Ex-IM Bank.

The conversion of AID's commodity import programs to a cash transfer is another diminution of U.S.-flag tonnage available for the U.S.-flag industry.

Before looking toward the extension of cargo preference to new areas, our concern is that we need to focus on the existing statutes and develop ways to ensure that Federal agencies are in fact complying with the current cargo-preference laws, which we think will result in substantial new opportunities for U.S.-flag liner operators.

Roger W. Wigen, "Impact of Liner Cargo Policies: Shipper Perspective"[18]

First, let me thank the Technology Assessment Board and the Office of Technology Assesment for the opportunity to participate today and give one shipper's viewpoint on the "Industry Impacts of Liner Cargo Policies."

Second, let me share some statistics on 3M's international trade. Since 1951, 3M international sales have grown from $20 million to $2.5 billion per year. In 1983, 3M international operations contributed about 36 percent of our $7 billion in corporate sales. We have operations in 52 locations outside the U.S. and manufacturing plants in 31 foreign countries. About 36,000 of our 85,700 employees are employed in international operations outside the U.S..

3M United States is one of several sources of supply which contributed to 3M's international market growth. In 1983, 109 million pounds, 6.6 million cubic feet, and 5,700 containerloads were shipped by ocean liner service from the United States to 116 countries at a transportation cost of $9.6 million. By contrast, in 1983, we imported 73 million pounds by ocean service from 27 countries at a transportation cost of $3.6 million. Indeed, we are involved in international trade and the world is our marketplace.

Next, let me add that coming from the private business sector, I am inclined to consider the basic issue to be economic and the question to be answered, how and to what degree market competition, cost, and efficiency should be applied in liner cargo policy. While that is my inclination, I recognize that maritime policy must also consider politi-

---

18. Transportation Manager, Regulation and Legislation, 3M Company.

cal, merchant marine, and national defense questions and is indeed a complex subject.

U.S. maritime policy has provided a semicompetitive environment, supported the right of carrier entry, prevented significant abuse of market power, promoted the U.S. merchant marine, preserved the American shipbuilding industry, recognized national defense, and functioned independent of the international practices of other countries. While FMC has carried out the economic surveillance and regulation activities provided by the Shipping Act, promotion of the U.S. merchant marine, national defense, and international practices of other countries including cargo preference issues have come under the purview of the Departments of Transportation, State, and Commerce. Consequently, bilateral agreements with anticompetitive implications have sometimes been established without regard for and conflicting with FMC objectives and responsibilties. There is a definite need to fine tune U.S. policy to balance both the national and competitive enterprise interests, and to clarify the responsibilities and involvement of various Government agencies.

The international convention, the UNCTAD Code of Conduct for Liner Conferences, has been described as a non-self-executing treaty. Its framework includes very weak mechanics for settling disputes, and it advocates closed conferences and cargo sharing.

Closed conferences, cargo sharing, bilaterals, and any other entry control or cargo-preference schemes breed anticompetitive barriers, complacency, inefficient operations, subsidy of inefficient carriers, and ultimately inequitable shipping prices for exporters and importers. 3M, and most shippers, oppose such policies and support free competition with cost, service, innovation, and customer trade requirements deciding share of business between conference and nonconference carriers.

Shipper experience in trades with cargo preference and controlled entry bear out these convictions. For example, shipping a container of cargo from the Midwest to Argentina and Brazil via Europe costs about $3,400, compared to about $5,000 per containerload direct from the United States. Carriers and conferences have not been willing to correct this inequity.

By contrast, trades without entry control and cargo-preference limitations provide innovative, cost- and service-efficient opportunities for both carriers and shippers. For example, 3M previously imported rubber in bulk from Malaysia to West Coast ports, then in box cars to our plant in Chicago. Containers for our exports from St. Paul to Japan were supplied and moved empty from Chicago. Through the efforts of a progressive

U.S.-flag carrier and our mutual interest in transport efficiency and carrier equipment utilization, we now import rubber from Malaysia in containers through to Chicago, load the same containers with domestic goods to St. Paul, and use the same containers for exports to Japan.

For the past several years anti-trust immunity, fixed rates, traffic pools, cargo sharing, loyalty contracts, open and closed conferences, mandatory independent action, shipper councils, service contracts, and other liner transport subjects have become household words on Capitol Hill. This year carriers, shippers, Government agencies, legislators, and the Administration working together reached a compromise maritime reform plan, and a new Shipping Act of 1984 was signed into law on March 20, 1984. FMC with record speed initiated rules to implement the new Act.

The new law and FMC rules are to provide liner conferences more freedom of action and encourage carriers and shippers to devise new innovative business relationships to lower costs and improve service. It is far too early, however, to conclude what and to what degree benefits will be forthcoming.

Most shippers, including 3M, are glad the many years of maritime reform discussions are over and anxious to address the new statutes and what must be done to make them work. Shippers do recognize several benefits from the joint dialogue preceding passage of legislation and in the new law itself. These benefits are:

- Government, carriers, and shippers did reach a compromise. Heretofore, each party was somewhat unwilling to sacrifice self-interest for the mutual benefits of all parties.
- Government agencies and legislators in the process became much more knowledgeable on maritime transportation issues and the needs of both carriers and shippers.
- Statutes and export/import shipping rules of practice have been clarified. Anti-trust immunity, prohibited acts, FMC jurisdiction, contracts, independent action, and intermodal rates are all more clearly defined. The new general standard is a practical improvement.
- Further review has been sanctioned with the directive for the FMC to assess the marketplace impact on carriers and shippers. Needed improvement and/or further deregulation or clarification can be considered.
- The agreement process and other FMC jurisdictions have been fine tuned and streamlined. Less FMC fiddling and more legitimate and defined monitoring are apparent.

- Open conferences have been preserved and conferences are permitted to set intermodal rates, allow carrier/shipper service contracts, and provide the right of carrier independent action.

However, most shippers also have some concerns. Several are:

- The new Act allows carrier or conference agreements that fix rates, pool revenues, restrict sailing and volume capacity, and prevent competition. Thus, the potential exists for significant constraints on the natural forces of a free competitive transportation marketplace.
- Service contracts and independent action thereon have been left up to the discretion of conferences. Conferences have not and may decide not to allow them.
- Confidentiality of service contracts is very much overstated. From a practical standpoint, nothing in a contract is likely to remain confidential.
- Without independent action, at least a degree of confidentiality, and/or nonconference competition, the incentive for and benefits of service contracts are significantly reduced.
- Five years, the mandate for FMC assessment of marketplace impact, is a long time to wait for amendments to remove or adjust constraints and/or inequities.

From the shipper's viewpoint, the outcome will depend to a great extent on how conferences and carriers respond to the freedom of action authorized by the new law. Is the new law and reform a "cure all" for the maritime industry and U.S. international trade? Is it a simple solution and formula for economic, political, merchant marine, and national defense interests? I submit that it is *not*, and that there is no simple solution. Maritime and international trade questions are easy to raise, but difficult to resolve, and it takes time.

The new law is a start, but if we are to continue toward improved conditions and a policy satisfactory to all interests, several issues will again have to be addressed in 1985 and succeeding years. They are:

- What must be done to make our policy more clear and consistent?
- How must we align Government agency responsibility to assure input from all interests?
- Will we need more regulatory reform and to what degree?
- What is needed to improve the health of our merchant marine?
- Can we separate economic, political, merchant marine, and defense considerations?

- Can the forces of a free marketplace function properly in the international maritime arena?

The real issue then, from my viewpoint, is whether our policy and new law will enable carriers to make a profit and provide needed capacity, *and* allow shippers the free flow of trade and cost competitive service. The degree to which natural economic forces can and will function in an international arena will have strong political, merchant marine, national defense, and foreign relation implications.

Let me conclude with these suggestions:

- Test the natural forces of the free marketplace and further reduce regulation.
- Separate free flow of trade and military auxiliary objectives.
- Discourage closed conferences and cargo sharing and preserve free entry and independent carrier action.
- Remove any inequities and restrictions that prevent legitimate U.S.-flag business management and market competition.
- Assure routine Government interagency dialogue and agreement beforehand on conflicting economic, political, merchant marine, and defense issues.
- Encourage and demand joint carrier, exporter-importer, and Government solutions to international trade and merchant marine policy considerations.

The doors of Capitol Hill and agencies responsible appear more open than ever before to consider further modifications if necessary to foster U.S.-flag and private enterprise growth in international trade.

Shippers are now also very eager to contribute. The National Industrial Transportation League's International Transportation Committee, of which I am Chairman, follows all maritime developments closely for over 1,500 shippers and transportation-related interests. The League was very active and instrumental in the compromise that led to enactment of the 1984 Shipping Act.

Another group of shippers, SCOT, which denotes Shippers for Competitive Ocean Transportation, is especially concerned about and dedicated to the issues of bilateral agreements, cargo preference, protectionism, and any other non-competitive constraint on maritime transportation and trade. As a member of the SCOT Steering Committee, I assure you that we are anxious to make whatever contribution we can to help shape U.S. liner cargo policy. We have been meeting regularly with the U.S. and foreign delegations to assure that the essential procompetitive concerns of shippers are considered in any intercountry agreements.

Your forum today is another step in the right direction. Again, my thanks for the opportunity to participate.

Sam Nemirow[19]

It is a pleasure for me to be with you today on behalf of the Council of American Flag Ship Operators to speak on the issue of cargo preference, specifically as it affects the liner sector.

In sitting down and thinking about these remarks, I couldn't help but notice that this was the 30th anniversary of the passage of Public Law 664 (P.L. 664) and the 80th anniversary of the 1904 Act, and that I hadn't been invited to any celebrations to mark these events. I think it tells us, notwithstanding how important these laws have been to our maritime industry, that none of the laws in support of our industry has been more controversial than cargo preference. To put this in perspective, I simply have to ask, particularly as it relates to the liner segment of the industry, why the controversy?

As Bonnie Green said, cargo reservation of Government-impelled cargoes — and by that I think we all mean cargoes that would not move but for the participation of the Government — goes back to 1904 when the Government reserved military cargoes to U.S.-flag [carriers]. Actually, from my reading, it seems that the only reason the policy is not older than that is because we did not ship seaborne military cargoes until after acquiring possessions in the aftermath of the Spanish-American War.

Next was the passage of the 1954 Act, P.L. 664, an Act which was decried by a number of our foreign friends, many of whom wished to continue carrying this cargo. The charge was made that the United States had become protectionist. Again, I fail to see the controversy. This is Government-generated cargo, and the law was nothing but an extension of the age-old principle that the shipper may select the carrier.

The 1954 Act was enacted largely to allow U.S.-flag vessels to participate in the business on the theory, as Senator John Marshall Butler of Maryland, sponsor of the legislation, said, that while we do not object to giving away U.S. goods, at last we are reserving the privilege of attending to the transportation.

Likewise, we find that around the world various forms of cargo reservation are the rule, not the exception. What does make the program controversial is its alleged cost. Again, speaking on the question of liner participation in the program, this, too, is ques-

---

19. Council of American Flag Ship Operators.

tionable. Liner cargoes subject to the requirement of P.L. 664 — and in this case we can also talk about P.R. 17 and the 1904 Act — are generally smaller lots moved in some packaged form (bag, box, etcetera); they are not easily suited to bulk transportation, or in all likelihood they would move on bulk carriers.

All U.S.-flag liner operators are conference-minded and maintain conference membership wherever they can. The rate they charge does not normally vary from the uniform market rate set by the conference. Consequently, this is a maritime program which aids U.S. carriers, but in effect at little additional cost to the Government.

I would also like to point out that the Government, notwithstanding the requirement of law, does have some loyalty to the U.S.-flag fleet. For example, the report entitled *Economic Effects of Cargo-Preference Law*, which was published by the General Accounting Office in January of [1984], quoted the Defense Department as saying that they would use U.S.-flag ships as much as possible [even if] were there no laws requiring it to do so. DOD accounts for 71 percent of the Government liner cargoes, according to that report.

That report also speaks to the costs to the Government in the liner sector under the P.L. 480 Title II program. The report concludes that, "On average, U.S.-flag liners cost 73 cents per ton more than foreign-flag liners, or an additional $600,000 in 1980."

My point here is that Government cargo reservation is neither new nor an unfair intrusion into the market, nor, in the case certainly of liner cargoes, is it even that expensive to the Government.

On the other hand, it may be useful to review the issue from the opposite perspsective, and that is that of the liner operator. Here I would like to quote from Admiral Holloway in a recent statement before the House Merchant Marine Committee:

> U.S.-flag preference for Government-impelled cargoes is absolutely essential for liner operators. First, it puts them more nearly on competitive parity with their foreign-flag competition, who generally carry all or nearly all of their own government-impelled cargoes; second, these cargoes act as seed cargoes making possible the regular sailing of U.S.-flag vessels on fixed routes with regular schedules, in parts of the world where this would otherwise not be economically feasible. . . . This is so because, where U.S. Government aid cargo is moving, it is frequently the majority of the outbound cargo in the trade.

I think these are significant points. The fact is that foreign governments generally by law or by custom book public cargoes on their own vessels, and that we are doing nothing exceptional in this regard. Cargo reservation is, of course, the trend today, not the exception.

In addition, this cargo block affects the rates and cargo mix of all U.S.-flag companies eligible for the program. The 1984 GAO report cited figures from 1980, but they are worth reexamining. In the liner category, the total cargo was 20.2 million long tons. Of this the Government concentration was 6 million tons, or 30 percent of the total. As I said earlier, 71 percent of this cargo was DOD cargo, and 18 percent was AID cargo. Again, however, the point is that, as those familiar with liner shipping realize, this block of Government cargo gives the U.S. carrier greater pricing flexibility and ultimately, we believe, more commercial cargoes.

Finally, the program has had its greatest impact on outbound voyages, where on some routes, as Admiral Holloway indicated, a majority of the outbound cargo is Government-impelled. To put that in perspective, when we look particularly at last year and the balance of trade of the United States, when the value of the dollar has driven the economy toward imports and away from exports, the outbound cargoes are most significant to the viability and health of the U.S. liner industry. These programs, these various laws, have filled many a container slot that otherwise would have gone empty.

From a policy standpoint, the fact is that in the liner sector the reservation of Government-impelled cargoes at a relatively modest cost to the Government has resulted in a better and more modern U.S.-flag fleet, more seagoing jobs, and ultimately more revenue for the Government itself.

Peter Luciano[20]

As I had planned to be an observer rather than a participant on this panel, I do not have a set of prepared comments. For that reason I would like to speak not on behalf of the member companies of the Transportation Institute, but [in order] to offer my personal view about a couple of matters that I would like to suggest affect not only the liner segment, but also the bulk segment — perhaps the general problem confronting these panels today.

I think at the heart of what we are discussing is the fact that the U.S. Government is unable to decide whether the merchant marine is a commercial or a Government activity. We see this in the organization of the executive branch with respect to the merchant marine, where responsibilities seem to fall somewhere between the Department of Transportation and the Department of Defense.

---

20. Transportation Institute.

Most countries view their merchant fleets essentially as government activities, even if they do have various commercial events, formulas, structures, and so forth. I don't mean purely in nationalized fleets or government-owned fleets, but also in the various forms of assistance that are provided directly and indirectly to merchant fleets around the world that most of you are familiar with.

On the one hand, in the United States, we speak of the merchant fleet as being a commercial activity. The Administration urges greater competitiveness in the merchant fleet — and I think that is a valid objective; the industry can be more competitive, and I think it has been for some time moving to become more competitive. However, I believe this thrust of more competitiveness, this admonition of more competitiveness, has tended to focus the issue as if it were purely a market problem, and that the solution were to be purely a market solution. In my view, however, there cannot be a real market solution if other governments do not allow market solutions in a number of very important trades, and if they in fact may not be willing to do so.

On the other hand, in this country, we speak of the merchant fleet in national security terms. The industry has always based its urgings for more active Government interest in the industry on the national security requirement for a U.S.-flag merchant fleet. And the Defense Department's participation in the deliberations of this workshop suggests the validity of the defense argument for a U.S.-flag merchant marine.

Some of the stronger U.S.-flag companies, in both the liner and the bulk trades, may be able to survive commercially in the absence of an increased and redirected Federal Government focus on the industry. But the question, I think, from the national policy point of view, is whether that remaining fleet in those liner and bulk sectors will be adequate for U.S. national interests as a whole.

In many trades, U.S. companies simply cannot compete regardless of how much more efficient they become. As Mr. Goldstein indicated in his remarks this morning, even apart from direct labor costs, which generally are targeted as a major problem in the operating part of the industry, and legitimately so — even in that area the peripheral cost of doing business under the U.S. flag would eliminate most U.S. carriers in a purely market environment.

So what is the net effect? In my view, the Defense Department has already described the net effect. DOD is in effect building its own in-house fleet, and it is doing it at the cost of many billions of dollars. I am not suggesting that there isn't a place for an in-house Defense Department sealift capability. The question is just how much and how

far do you want to go. Do you want to usurp the entire area of economic activity where today there is commercial activity under the U.S. flag? Ultimately the question becomes, is it cheaper to operate a Government-owned fleet than it is to operate one under a commercial regime.

If we arrive at a decision by default, through the failure of the Government to address some of these basic issues, then I am concerned that one day soon we will in fact see a largely nationalized fleet, maintained at great Government expense. Then one day someone will come along and suggest that there are inherent inefficiencies in having the central Government operate what is essentially a commercial activity, and will suggest that we should deregulate and return this activity to the private sector.

I think you have to accept this eventuality, if you believe in capitalism, if you believe in free enterprise. If you don't, if you believe the Government can operate these activities at lower cost and more efficiently than the private sector, then I think you would have to reject the call for free markets, for free enterprise and so forth. However, I think that is alien to almost all of the basic premises that we apply not only to this industry, but to American industry at large.

I think at the point where there may be no U.S.-flag companies left, we will find that the cost of reconstructing the fleet, not to mention the interim costs of building and operating a Government-owned fleet in the meantime, will have proven to be both prohibitive and wasteful.

What I would like to suggest today is that before we make this decision by default, before we allow the dual personality of the fleet to confuse us as to whether it is free market policy or defense policy that should guide national thinking on this matter, that we should look at the true long-term cost and benefits of this problem, and change course at this point.

Thank you.

PANEL ON INDUSTRY IMPACTS OF BULK CARGO POLICIES

December 3, 1984

PANELISTS

George Berg
American Farm Bureau Federation

Gus Caras
Ogden Corporation

Jack Goldstein
Overseas Shipholding Group

Kenneth Kastner
Chemical Manufacturers Association

TOPICS FOR DISCUSSION

1. Effects of current U.S. cargo-preference laws and regulations on levels of trade and on U.S. bulk operators and shippers, including estimates and projections of costs and benefits.
2. Impacts of any increased cargo-preference requirements, imposed either by U.S. actions or by our trading partners; trends toward and effects of commercial bulk cargo-preference laws.
3. Prospects for and impacts of an UNCTAD bulk code or other multilateral or bilateral agreements on bulk cargo policies; prospects for UNCTAD efforts to phase-out open registry.
4. Impacts of existing and future cargo policies on U.S.-controlled, foreign-flag operators.

SUMMARY OF DISCUSSION

Industry Conditions and Prospects

Industry representatives on the bulk shipping panel pointed out that the entire bulk shipping industry worldwide is extremely depressed and is expected to continue to be in the foreseeable future. Rates are not expected to justify new building at least through the end of the decade. U.S. carriers are in even worse condition, with operating costs $2 million per vessel per year higher than those of foreign competitors, but even low-cost operators are going out of business. In the past, conglomerates found it profitable to have shipping subsidiaries; but today many are being spun off, both because current rates cannot justify needed investment and because, with low inflation, there is no benefit in holding physical assets in the expectation of appreciation.

Little optimism was expressed. U.S. bulk operators cannot compete and the U.S. Government is not helping to improve the situation. Operators believe that most Americans do not appreciate the extent to which foreign countries subsidize their fleets.

Direct cargo-preference is not typical, but aid is available in many forms. Shipyards frequently are nationalized, and below-market financing may be offered for ships purchased from national yards. Governments may also provide tax incentives for shipping on national flag carriers.

Three possible forms of subsidy for the U.S. maritime industry were cited: construction and/or operating aid; a Government build-and-charter program; and cargo preference. The panelists felt that the United States must define its shipping needs, then take steps to assure the needed fleet. They urged that existing cargo-preference laws should be implemented fully. They also suggested that the Government might exclude from U.S. ports foreign ships built at costs that could reasonably be described as "dumping" levels.

Defense-Related Issues

National defense requirements were discussed in some detail. The primary requirement is for small product tankers.[21] Sufficient tonnage now exists in the "U.S. effective control" (USEC) fleet of U.S.-owned foreign-flag ships, in the panel's opinion. However, some participants expressed concern about the number of usable tankers: most of the USEC tanker fleet is made up of large crude oil carriers, which may not be as useful militarily as smaller oil-product tankers. Because of consolidation in the world petroleum industry, furthermore, the tanker fleets of U.S. oil companies and of our NATO allies are declining in size and significance. A separate point raised by shipping interests was the cost of defense-related features of their fleet and whether these costs should be borne by U.S. taxpayers, rather than a small number of shippers.

While the panel provided no real answers to the plight of the U.S. bulk fleet, the "Japanese solution" was described as a possibility. In Japan, shipping is just one component of an overall business venture. If a major project to export a commodity is contemplated, everything from the manufacture of the item to the transportation system is planned as a whole. The government is involved from the start and tailors its aid to the specifics required, probably including subsidizing such items as interest rates and crew costs. The consequence is that Japanese-flag ships carry 50 percent of Japanese bulk trade, even though Japan is no longer classified as a low-cost carrier.

---

21. Tankers which carry refined petroleum products, such as gasoline, diesel, fuel oil, etc.

Cargo Reservation and Preference

The panel also discussed the possibility of an UNCTAD bulk code, with the general reaction that it is unlikely to happen. Many LDCs are less interested in pushing for a bulk code because they no longer perceive that it would be in their interests. Many of these nations simply do not have the wherewithal to build and operate commercial fleets. In addition, there is clear opposition on the part of most OECD countries. Bulk trade, unlike liner trade, is not over established routes on a regular basis. Rather, bulk trade tends to be "round the world," with contract carriage of a specific cargo from one place to another. This does not lend itself to bilateralism. Further, some bulk vessels, such as parcel tankers, are dedicated to carriage of specific cargo and must be used wherever that trade is at the moment. U.S. bulk cargo-preference was discussed at length by shippers' spokesmen. They oppose cargo-preference and spoke emphatically in opposition to any expansion of preference laws. Statistics were presented on the increased costs of agricultural exports which would result under commercial cargo-preference. If a 20-percent preference had existed in 1982, agricultural export costs would have risen over $1 billion. If U.S. goods are to be competitive and U.S. farmers to make a profit, transportation must be at the lowest possible cost. The current U.S. trade deficit makes it even more imperative that U.S. exporters not be burdened further with higher transportation costs.

In general, this panel — or at least the maritime industry participants — were far less sanguine about the industry's prospects than were their liner counterparts. New and innovative proposals will be needed if the U.S.-flag bulk fleet is not to disappear altogether.

PANELISTS' PRESENTATIONS

Jack Goldstein[22]

When we talk about U.S.-flag bulk shipping participation in the foreign trade today, I think we are talking about something that is illusory and at the same a little bit confusing. In the few minutes I have today, I would like to discuss some of the prevailing illusions.

First there is an impression that an American-flag operator, or a North European operator for that matter, can be competitive in the bulk shipping markets with a low-cost flag. Today the cost differential for the cheapest nonunion U.S.-flag crew, or a

---

22. Overseas Shipholders.

cheap union crew for that matter, would be at least $2 million a year. This is $2 million a year in excess of the market rate that is not now compensatory for the lowest cost operator in the world. The lowest cost operator is hemorrhaging money today. An example: in the past 6 months, something like 250 ships, mostly bulk ships, have been arrested for nonpayment of bunkers — the owner can't meet his expenses. A number of major bulk operators have gone out of business, have been bankrupt, from Taiwan, Korea — the list goes on.

This situation has persisted now for the better part of 10 years, so we are not talking about a cyclical change. We are talking about a semipermanent, long-term condition that can only be coped with over a very, very long period of time. The economic expansion that we have experienced in the last 2 years has not made a significant difference in the situation.

A second impression or illusion is that the U.S. bulk fleet is highly protected in the international trade, while many national flag fleets are free-market-oriented, competing vigorously with each other. That is generally not the case.

The U.S. fleet is protected in the cargo-preference trades, but in total they employ about 40 to 50 bulk ships. There are something like 7,000 bulk ships in the world, so we count for virtually nothing.

If you look at the major national-flag fleets, the cross-traders like Norway, the British, the Japanese, one way or another they are directly or indirectly beneficiaries of government support. It is difficult now to think of one significant European shipbuilder that is not directly owned by the local government. You have Italian shipbuilders, you have Spanish, all government-owned — the product of insufficient business and the fact that the shipyards in these countries are no longer competitive.

In Japan, where there is no cargo preference, the fleet manages to prosper relatively, not in a financial sense but in terms of size. The government promotes both shipbuilding and ship operation of Japanese-flag vessels directly, through the Ministry of Trade, through very advantageous credit facilities.

A third illusion is that there is a U.S.-flag bulk shipping policy. Actually what we have is a mixture of individual statutes, subsidy contracts, contract changes, rules and proposed rule-makings. One could talk about stability in U.S.-flag cargo-preference policy — that is, no growth, no decline — but in reality there is total confusion and uncertainty about what that apparent policy means.

One good example is the Title XI program that provides Federal guarantees for ship mortgages. Today a tanker owner cannot receive a Title XI guarantee from the Federal Government because the agencies repsonsible for the policy don't know where those policies are going in the next 6 months or next year. Because there is uncertainty about the policy, the Maritime Administration is unwilling to guarantee a tanker mortgage.

Fourth, there is another unfortunate impression widespread among cargo interests in the United States, that any program that would aid the bulk shipping industry must necessarily damage cargo interests. I don't think it's the case. It shouldn't be the case, and I don't think a program that would injure the agricultural industry or the coal industry could pass. So it could not be the case. It's not impossible to fashion a program that does not damage those interests, and, at the same time, allows for some support of what is really a nonexistent bulk shipping industry.

That is another obvious illusion, that we do have a bulk shipping industry. Aside from this relatively small volume of preference cargo, there are all of about a dozen tankers under U.S. flag, built and operated with subsidies, that are trading in the commercial market. This program, as you know, doesn't exist anymore; there will be no additions to those ships. They were virtually all built 10 years ago when the tanker market was in some semblance of balance. There have been no contracts made for the past 10 years.

A question was sent to us about the impact of commercial cargo-preference requirements on foreign-flag fleets or on the U.S. fleet. Generally, preferences are not overt overseas. There are some cases, as in France or Spain or some of the OPEC countries, where you do have overt flag preferences. More generally we are talking about preferential arrangements between governments and shipowners involving financing. An example would be the program in Japan a few years ago to provide 2-percent mortgages to Japanese-flag ship owners. Interest rates in the United States at the time were about 18 percent.

There are also long-term charter arrangements between government agencies or even private parties, very long-term arrangements — we are talking about 15-year charters — combined with low-cost financing to offset the high cost of national-flag operation. This is true in Japan, but it is also true in some places like Norway and many of the other countries I mentioned.

For the United States, anything we develop in this area would be from a base of almost zero. We are starting from scratch. That's a problem but it's also an opportunity in that ship prices, both new vessels as well as existing vessels, are much lower overseas.

Gus Caras[23]

Thank you. It's always a pleasure to follow Jack because he does so much of your work for you. However, I would like to add a few remarks. Considering the depressed state of the market that we have been in for the last 5 or 10 years, I think it's a tribute to the industry that we are as resilient as we are and we are still here.Today we do have some particular issues that face us that I think we have not had before, which add to the problem. In the tanker market, for example, rates are at such a level that no one predicts rates that would justify new building for the foreign market before the end of the decade. As to the dry bulk trades, nobody ventures even a guess at this point.

Shipyard employment is down worldwide. The Japanese for the first time within memory are now looking for work; they are looking into joint ventures with the People's Republic [of China] as a way of keeping their yards open.

In the United States, as we all know, shipyard employment is down; we went from a backlog of $4 billion in the mid-1970's to the situation today where there are two commercial vessels now under construction, and that's the extent of the backlog in the United States. As to the Navy work that exists, it's unfortunate, but 80 percent of the work is concentratd in six shipyards.

So across the board the maritime industry both worldwide and in the United States is experiencing severe problems. We all know the statistics. Today the United States has the eleventh largest fleet in the world; in 1950 we were the first. Today we import less than 3 percent of our dominant bulk commerce on U.S.-flag vessels.

A second troubling feature is the trade deficit. Over the weekend we read that we are now at $100 billion and that in the very near future many experts predict the trade deficit will hit the $150-billion mark. This certainly does not augur well for U.S. shipping.

During the late 1960's and 1970's, there was a tendency for U.S. shipping assets to become concentrated in the hands of a few conglomerates. What we have already seen in the 1980's is a reversal of that situation. It's not surprising, in view of current market conditions, that we have seen the spinoffs of the last several years. My company, the Ogden Corporation, for example, spun off its bulk shipping company, OMI. I don't know what the reasoning was for the others, but in our case there were basically two reasons:

---

23. Ogden Corporation.

one, we could not see in the near term or in the distant future rates that would justify the substantial investment that a shipping company calls for these days; and, secondly, with the disappearance of inflation, one was robbed of the opportunity, at least, to hold on to assets which were appreciating.

So where does that leave us? Well, as to the U.S. bulk market there are some additional troublesome considerations. In the area of national security, various DOD scenarios put the U.S. fleet and the vessels available to the Department of Defense as marginally adequate if there is a NATO type of war.

As Jack indicated, we are seeing scrappings at a rate of 20 or 30 this year. We are now at the point where even under the most tenuous of scenarios, as contemplated by DOD, we simply don't have the type of bulk vessel available that the DOD finds most useful, a 40,000- to 80,000-deadweight-ton vessel.

We have two additional problems in the bulk market that I might just mention briefly. One is the stability of the pension funds. We are in a situation now where we are beginning to wonder who the last man out is going to be, because he is going to inherit the job of funding the pension funds.

The other situation that is developing is the loss of tax revenues to the extent that we start to depend upon an offshore industry to service our needs. I think in the assessment of the Boggs bill [H.R. 1242, 98th Congress], for example, there was a conclusion that the construction of 20 vessels per year would bring in something like $400 million in tax revenues. It would be interesting to see whether the converse of that follows and to what extent the loss of U.S.-flag vessels to an offshore industry has a negative impact on the Treasury. Where does that leave us? Well, we all know the three basic broad-range approaches that have been tried before — subsidy systems, expanded cargo reservations in the commercial field, and the Government build-and-charter programs. In the interests of time I won't go down and talk about the pros and cons of these programs. As to the expanded cargo-reservation programs, we of course heard all the cons this morning.

The Government build-and-charter program was mentioned this morning as a possible thing to look at. The problem, of course, has been that the type of vessel that the Department of Defense wants to build is not commercially a very attractive vessel; and, secondly, DOD, at least up until now, has not been very anxious to use its own funds to build those vessels.

Does that mean that there is nowhere for us to go? I don't think so. I think there are some specific things that we can do, realistic initiatives which are consistent with established national policies. I think the Government, for example, should make the basic decision: it should define what our requirements are. I know DOD has several studies — last year there was a study which listed several scenarios of various types of war, and concluded what its requirements would be.

But I think we need something more broad-ranging; I think whether it's DOD, DOT, or at the White House, wherever it is, I think we need as a Nation to state what our requirements are, both in terms of shipping and shipbuilding. Once those requirements are stated, I think the rest will follow.

Secondly, as Bonnie Green and Sam Nemirow suggested, I think we ought to go back and tighten up the existing cargo-preference programs. The cash transfer program, for example, and the blended credit program — I think we ought to get a solid footing there. The representative from the Agriculture Department this morning said that Agriculture did not favor an expansion of cargo preference; at the same time, Agriculture does not favor a contraction of the cargo preference. That being the case, and assuming that is our national policy, then I think we ought to go back and tighten, as I said, the two programs, blended credit and cash transfers.

A third thing that perhaps we ought to think about is an initiative suggested by the Shipbuilders' Council several years ago, but which did not go anywhere. I have always thought that the idea merits more attention. This would be a policy to deny foreign-built vessels access to U.S. ports if one can prove that these vessels were built pursuant to dumping procedures. I know it's a difficult thing to do, but in the steel industry and many other industries, the idea of denying U.S. markets to foreign products which are being dumped into the United States is a policy which is clearly established. I see no reason why it can't be extended to the shipbuilding area. It's a lot of work, it's hard to prove, but I think it bears looking into.

Fourthly, when one looks at the bulk trades in which U.S. participation is the most efficient, I think clearly one comes up with the import of petroleum products. We all believe in a free market economy, but even Adam Smith several centuries ago agreed that there are occasions when a free market policy must step in the background and must give way to national defense requirements. At that time he stated that the flag of Britain should be used when the defense of the nation was threatened.

I think the same kind of thinking applies today. We have less than 3 percent of petroleum products being brought into the United States being carried on U.S.-flag vessels. We have a number of CDS-built vessels which are basically laid up or underemployed. The owners of those vessels are heard to complain that, notwithstanding the fact that the vessels were built with CDS, they are not efficient, they cannot compete on the world market. I think we ought to look at whatever it takes to keep the existing CDS fleet, built for the purpose of importing petroleum products to the United States, in a competitive posture. Whether it's in the form of additional subsidies, or credits of some sort — it's a quantifiable amount. It's not a broad subsidy or a brand-new program. I think we ought to look at that. We are talking about the CDS-built vessels that are now underemployed. I believe that some type of program should be adopted for those vessels.

One concluding remark I would make. It is true that the U.S. fleet is certainly not competitive vis-a-vis the foreign-flag vessels; our manning requirements, manning levels and manning costs, are much, much higher. However, we all know that as we speak now, we are all entering new contracts; we are bargaining. I think that what will come out is that you will see a substantial reduction of our manning costs.

George L. Berg, Jr.[24]

Farm Bureau is the largest general farm organization in the United States, with a membership of 3.3 million families in 48 States and Puerto Rico. It is a voluntary, nongovernmental organization and represents farmers who produce virtually every agricultural commodity. We appreciate the opportunity to present Farm Bureau's views on cargo preference and the impact cargo preference has on agricultural exports.

In January 1984, the elected voting delegates of the member State Farm Bureaus adopted the following policy:

> Since cargo-preference requirements make U.S. farm exports less competitive in world markets, we oppose any cargo preference legislation that applies to agricultural products. We also oppose the cargo-preference provision of maritime agreements, such as those with the Soviet Union and the Peoples Republic of China, which require that one-third of their U.S. grain purchases be transported on U.S.-flag vessels. Added costs of shipping on higher cost U.S.-flag vessels discourage U.S. commodity purchases and put the United States in the position of a residual supplier.

American agriculture cannot prosper without continued growth in foreign markets. We export the harvested products from two out of every five acres of cropland

---

24. Assistant Director, National Affairs Division, American Farm Bureau Federation.

because our productive capacity in agricultural crops is well beyond the ability of our domestic needs to absorb. In recent years, we have exported two-thirds of the wheat we produce, a similar percentage of rice, over half of our soybeans, a third of our grain sorghums, and one-fourth of our corns. A third of our tobacco and half of our cotton go to foreign outlets.

A recent study by the U.S. General Accounting Office showed that the Department of Agriculture, in 1980, had to pay an additional $58 million for P.L. 480 Title II programs (Food for Peace) that are bound by a cargo preference of 50 percent; and, as revealed by the North American Export Grain Association, in 1982 freight surcharges on P.L. 480 shipments amounted to almost $314 million, which could have been used to export an additional 2.0 to 2.5 million metric tons of wheat or about 2.9 million metric tons of corn. Under proposed legislation to raise cargo preference by 5 percent and then 1 percent per year until 1999, the transportation costs could increase from $40 to $80 per ton. This would add $387 million to the freight differentials over the last 5 years, and these additional costs would cripple the agriculture sector since agricultural exports would drop and consequently net farm income would be reduced.

The following economic analysis shows some of the likely impacts if cargo preference had been applied to U.S. cash export sales of corn, wheat, and soybeans in the 1982-83 crop year. The analysis presents two alternative applications of cargo preference: 5-percent and 20-percent cargo preference. Since moving grain and soybeans in U.S.-flag vessels is more expensive than using larger, more efficient foreign-flag vessels, three alternative scenarios of shipping cost differentials are presented. Alternative shipping cost differentials for bulk corn are assumed to be $40, $50, and $60 per ton. Alternative shipping cost differentials for bulk wheat are assumed to be $50, $65, and $80 per ton. Alternative cost differentials for bulk soybeans are assumed to be $60, $70, and $80 per ton.

A 5-percent cargo preference in effect in 1982-83 would have required almost 6 million metric tons or 226 million bushels of U.S. grain and soybean exports to be shipped in American-flag vessels. A 20-percent cargo preference would have required 24 million metric tons or 905 million bushels of U.S. grain and soybean exports to be shipped in more expensive American-flag vessels in 1982-83.

With a 5-percent cargo preference in effect in 1982-83, shipping costs would have likely increased by $286 million to $426 million. A 20-percent cargo preference would have increased shipping costs by $1.143 billion to $1.704 billion.

The average farm price of corn in 1982-83 was $2.68 per bushel; wheat was $3.55 per bushel; and soybeans were $5.69 per bushel. Taking these average farm prices as given, the additional shipping cost resulting from a 5-percent cargo preference is equivalent to 61 million bushels of corn, 48 million bushels of wheat, and 19 million bushels of soybeans. The additional shipping costs for a 20-percent cargo preference translates into 245 million bushels of corn, 192 million bushels of wheat, and 75 million bushels of soybeans.Given the competitive nature of the agricultural and grain industries in the world, the increased shipping costs would not be passed on to the foreign buyer. Foreign buyers would purchase needed agricultural commodities in the world market at competitive prices without paying the additional transportation charges. Thus, the world market place would force domestic grain prices in the United States to remain competitive. The increase in shipping costs would then be transferred back down the marketing chain to U.S. farmers in the form of reduced exports. Competitive forces in the U.S. economy would cause the resulting reductions in agricultural exports to lower farm prices for grain and soybeans. Lower farm prices would decrease farm income.

It is important to note that the reduction in agricultural exports would have a multiplied effect on farm prices. That is, by reducing exports, the U.S. farm economy not only loses out on the sale of agricultural commodities to foreign buyers, but the farm price is reduced by a multiple amount, over and above the increase in shipping costs. For example, past experience and research indicates that a 100-million-bushel reduction in corn exports will reduce the season's average price of corn by $0.17 per bushel and the season's average price of soybeans by $0.22 per bushel. A reduction in wheat exports of 100 million bushels will reduce the season's average price of wheat by $0.32 per bushel and the season's average price of corn by $0.07. Reductions of soybean exports of 100 million bushels will decrease the season's average price of soybeans by $0.70 per bushel and the season's average price of corn by $0.15 per bushel. In contrast, the increase in shipping costs, when averaged over 1982-83 estimated grain and soybean production with a 5-percent cargo preference rule in effect, would range from $0.01 to $0.02 per bushel of corn, $0.04 to $0.06 per bushel of wheat, and $0.03 to $0.05 per bushel of soybeans. The increase in shipping costs with a 20-percent cargo-preference rule in effect would range from $0.05 to $0.08 per bushel of corn, $0.15 to $0.24 per bushel of wheat, and $0.14 to $0.18 per bushel of soybeans.

Additional shipping and transportation costs associated with cargo-preference regulations are likely to be divided unequally between farmers and foreign buyers. However, if all of the increased shipping costs associated with a 5-percent cargo-

preference requirement were passed on to the farmer in the form of reduced exports, and these export reductions came during the 1982-83 crop year, the season's average price would be reduced by $0.07 to $0.10 per bushel for corn, $0.10 to $0.15 per bushel for wheat, and $0.10 to $0.13 per bushel for soybeans. If a 20-percent cargo preference was applied, the season's average price would be reduced by $0.28 to $0.42 per bushel for corn, $0.38 to $0.61 per bushel for wheat, and $0.39 to $0.53 per bushel for soybeans.

Lower commodity prices would have had a direct and predictable negative impact on grain and soybean producers. For example, since corn production in 1982-83 was 8.2 billion bushels, the $0.07 to $0.10 per bushel lower price would decrease income to corn producers by $574 million to $820 million with a 5-percent cargo preference. The $0.28 to $0.42 per bushel decrease in corn price with a 20-percent cargo preference would have reduced income to corn producers by $2.3 billion to $3.4 billion in 1982-83. The wheat crop was 2.8 billion bushels in 1982/83. Thus, the $0.10 to $0.15 per bushel lower wheat price with a 5-percent cargo preference would decrease income to wheat producers by $280 million to $420 million. A 20-percent cargo preference would reduce wheat producers' income by $1.1 billion to $1.7 billion, due to the $0.38 to $0.61 per bushel price reduction for wheat. With 1982-83 soybean production at 2.3 billion bushels, income to soybean producers would be $230 million to $364 million lower because of the $0.10 to $0.13 per bushel lower price, assuming a 5-percent cargo preference. The $0.38 to $0.53 per bushel decrease in soybean price with a 20-percent cargo preference would have reduced income to soybean producers by $0.90 billion to $1.2 billion in 1982-83. The total reduction in farm income resulting from a 5-percent cargo-preference requirement on grain and soybeans ranges from $1.084 billion to $1.604 billion. A 20-percent cargo-preference requirement on grain and soybeans would cause farm income to decrease by $4.257 billion to $6.371 billion.

Reduced exports and lower farm prices would have a major impact on the cost of Government programs. Government farm program costs would have increased in 1982-83 if cargo preference was applied. Cargo-preference schemes already in effect cost American agriculture and U.S. taxpayers in general, millions of dollars annually. As farm prices are further discounted by cargo-preference rules, Government storages and deficiency payments will increase. The Government's cost of applying cargo preference to cash or commercial exports would increase the burden on taxpayers for farm price and income supports.

Based on this economic analysis, cargo-preference rules should not be applied to the blended credit program or to any future export payment-in-kind (PIK) sales. If the

export PIK program provision and the blended interest export program are to be effective, it is essential that these programs be given the opportunity to accomplish their original objectives. Applying cargo preference to these programs would completely nullify their effects, because cargo preference will raise the cost of buying U.S. commodities and substantially reduce U.S. agricultural exports.If cargo preference is applied to agricultural exports, the two hands of the U.S. Government would be operating in opposition to one another. The Government would be using one hand to increase and promote agricultural exports through the blended credit and export PIK programs. The proverbial other hand would be setting the stage to substantially reduce agricultural exports with cargo preference. It does not make economic sense to implement such requirements at a time when the United States needs to become more competitive and aggressive in obtaining better foreign market access. One of the greatest risks in applying cargo preference is that after a few years, the United States would find its export markets severely eroded because cargo-preference requirements encouraged production in other exporting countries in the world, given price differentials.

Cargo-preference requirements would have adverse effects on the U.S. maritime and ocean freight shipping industries. Attempts to guarantee market shares and artificially maintain shipping costs without regard for the economic realities of world ocean freight costs only perpetuates the American fleet's inability to compete with foreign vessels by increasing the supply and reducing the demand for U.S. ocean transportation services. Subsidies to the shipping industry in order to protect the industry are no different than subsidies that guarantee farmers' prices above world competitive prices. Cargo-preference laws stifle the incentive to invest in newer, more cost-efficient vessels. Proposed cargo-preference requirements would continue the cycle of never-ending, more expensive subsidies and higher operation costs for the maritime industry, similar to [the effects of] Government protection of auto and steel industries. These higher costs and inefficiencies are devastating to U.S. competitiveness. Price-sensitive raw commodities like agricultural products, which must compete in a world market, are particularly vulnerable to this intervention. Both the maritime and the agricultural industries will function more efficiently and enjoy better long-term economic health if shipping markets are left free to allocate resources in response to actual, rather than artificially imposed, economic forces.

Mr. Chairman, this concludes my prepared remarks. I would be happy to answer any questions that you or other members of the panel may have.

Kenneth M. Kastner[25]

Since I am the last today, I will try to keep my remarks to what has not been said, and a number of them will pertain to the chemical industry and what is known as the parcel tanker fleet.

About half of all U.S. chemicals are transported on parcel tankers. Primarily they carry liquid chemicals but, to a certain extent, gas products are also put into the tanks. A typical parcel tanker is about 39,000 tons. It might have about 20 to 50 tanks per vessel, each being between 300 to 2,000 metric tons in capacity.

There are about 340 parcel tankers in the world today, and only about four operators serve the U.S. trades. None of these are U.S.-flag operators. For the most part, there are very few U.S.-registered parcel tankers in the world. This is primarily because of the high crew and
construction costs.

Today most of the time there is over-capacity in the parcel tanker business, and therefore a demand to have new parcel tankers or to build new parcel tankers may lead to a redundant use of resources.

The basic position of the shipper is that we should be free to choose the most competitive vessel that provides the best service that is available. We hold this principle very profoundly; it is a principle that we have to operate under in our industry, and we feel it is a principle that has led to making the economy of the United States as strong as it is.Even more importantly, I think, we see a huge trade deficit today, twice the size it was last year; we have to be very cognizant of any action that we take that will impact upon our ability to trade, and certainly the price we pay for transportation services will directly affect that. In turn, it affects the U.S. jobs and the level of our manufacturing in this country.

I would like to explain a few particular problems that the chemical industry would have if bills such as H.R. 1242 [98th Congress], the Boggs bill, or other cargo-preference bills modeled on that, were to take effect. What I think this shows is that, particularly with respect to the chemical industry — and I think it would apply to most other exports — the approach simply doesn't work in the way that we ship our products today.

First of all, the chemical parcel tanker does not offer a service that is fungible; it is not a container ship that will take any container that is left at the dock. There are

---

25. Chemical Manufacturers Association.

specialized tanks; each tank often has a different heating system, venting system, pumping system, cooling system. Often these tanks have to be dedicated to particular types of chemicals because of the hazards of the various chemicals and the requirements for shipping of those chemicals. Because of the special needs, the operator will often seek a fairly long-term commitment from the shipper so that the operator can recoup the cost of applying this special equipment. The shipments are subject to Coast Guard regulations and IMO regulations, and the crew has to be very experienced in how to handle the particular products at issue.

What this all means is that if there were legislation that would lead to the building of 15 new U.S. parcel tankers, it is unlikely that those parcel tankers would meet the shipping requirements of the U.S. chemical exporter. Also, even if you have some tankers out there that would meet the requirements, there likely will not be enough to provide service when necessary, so what you will have is chemicals sitting in terminals at docks, which can create a safety hazard, and also it will not meet the needs of our foreign customers for immediate delivery of products that are used their production.

We have done a study — actually it was done by a Bahamian broker of parcel tankers — as to the cost of operating a U.S. parcel tanker vessel versus a foreign-flag parcel tanker vessel, and we found that the U.S. costs are about 83 percent higher per year, primarily due to the construction costs and crewing costs. Of course, this would require the rates to be 83 percent higher per year to cover these costs.

Mention was made earlier of problems with cargo reservation in the liner trade to Brazil. CMA has done a study of that. We looked at about seven or eight randomly selected chemical products, and we found our costs are 19 to 134 percent higher from the United States to Brazil than from our major European competitors to Brazil. So the cost differential is significant and will have to be borne by the U.S. chemical shipper.

Now, in the chemical parcel trade, you often have varying demands on a year-to-year basis. For instance, today we have relatively few shipments to South America, primarily because of the debt problems and the import restrictions in South America. If you were to create a U.S. parcel tanker fleet through legislation, what would that parcel tanker fleet do when you have a drying up of U.S. bulk chemical exports to a particular trade? That fleet would have to be able to compete in other trades in the world, and that means they have to be competitive on a world basis, not just competitive by reason of U.S. subsidies.

Also, the chemical parcel tanker fleet tends to operate in a round-the-world type of trade, or a round-a-trade type of trade. Typical examples would be a vessel that spent 70 days at sea and visited 29 berths in 16 different countries; another one 75 days visiting 11 countries; and another 140 days visiting 17 countries (table 1). That is the typical type of operation.

Now, a bilateral approach or a cargo-preference approach is based on the notion that you go from the United States to a country and then return. That is simply not the way that chemical parcel operations occur today, and I think more and more we are seeing liner operations move to around-the-world type of trade. That is not well-suited to bilateral arrangements.

Again, the United States could subsidize through cargo reservation our fleet that operates from the United States to Brazil, let's say. Once it has to go from Brazil to the west coast of North Africa, and then from there to Spain, and then from there to Sweden and return to the United States, it's got to be able to operate economically in those foreign-to-foreign trade routes. Our subsidies would not be able to make up that differential.

One other point that was raised earlier was the precedent that cargo-preference legislation would set for U.S. efforts to dissuade foreign governments from imposing their own cargo preference and cargo reservation. This is a very real problem that CMA and the SCOT group have experienced first-hand in negotiations with foreign governments. We have been a shipper observer to these negotiations, and obviously those governments raise the point that if we have our own cargo-preference laws, why can't they? Well, it's a very legitimate argument. The problem is, of course, that while our Government cargo might be 6 to 10 percent of our trade, their government cargo ranges from 80 to 90 percent of the trade, because their governments are involved so much more in financing, guaranteeing loans on cargo, etc. They control most of the manufacturing facilities and therefore are the purchasers, or sellers, of the products, and, for the most part, the government cargo makes up the bulk of those trades.Every time we agree to a new cargo-preference scheme, covering what we think is a small portion of our trade, it sets a precedent for a foreign country to cover a very large portion of their trade. In addition, the CSG-U.S. talks are based on the notion that the United States will not increase its cargo-preference legislation. Their cooperation in mutually resisting cargo reservation by foreign countries depends on our good-faith approach of not increasing the cargo that we reserve to our own U.S. carriers. If we lose that cooperation by the CSG governments, then we may have more difficulty in standing up to the developing countries.

Table 1. — Cargoes and Routes for a Typical Chemical Parcel Tanker Voyage.

WESTBOUND ROUTE A

Europe Westbound via the United States to the Far East

Time of westbound voyage:	70 days
Total cargo carried:	40,000 MT
Parcels carried:	36
Ports of Call (berths 29):	15
Origin/Destination countries of cargoes:	16

(England, West Germany, Belgium, Spain, France, Netherlands, USA, Canada, Panama, [Canal Zone], Japan, Korea, Taiwan, Hong Kong, Philippines, Singapore, and Malaysia)

WESTBOUND ROUTE B (Vessels regularly operate on both routes)

Europe Westbound to Australia via the United States

Time westbound:	75 days
Total cargo carried:	28,000 MT
Parcels carried:	52
Ports of Call (berths 24):	14
Origin/Destination countries of cargoes:	11

(England, West Germany, Belgium, Spain, France, Netherlands, USA, Colombia, Panama [Canal Zone], New Zealand, Australia)

EASTBOUND ROUTE A (Typical return voyage for Westbound voyage A or B)

Time eastbound:	70 days
Total cargo carried:	43,000 MT
Ports of Call (berths 24):	12
Parcels carried:	29
Origin/Destination countries of cargoes:	7

(Indonesia, Philippines, Japan, Canada, USA [West Coast and Gulf], France, Rotterdam [parcels trans-shipped to several European countries on through bill of lading])

RETURN ROUTE B (Occasionally vessels on one of the above westbound routes will continue westbound to India, Saudia Arabia, and [via Suez Canal] to Greece, Italy, Spain and on to Rotterdam. Cargo details of an actual voyage are not available.)

A typical round voyage combining routes WESTBOUND A and EASTBOUND A would involve the following:

Time of voyage:	140 days
Total cargo carried:	83,000 tons
Parcels carried:	65
Ports of call (berths 53):	27
Origin/Destination countries:	17

SOURCE: Chemical Manufacturers Association

I agree with what many of the speakers have said today, that we really need to focus on our legitimate needs for a maritime fleet. It was mentioned earlier by Gus Carras that the free market should give way where there are legitimate defense needs, and I would agree with that. What we need to do is define those needs. I think there was some discussion of that today, tha. indicated those needs may not be well-suited for commercial vessels. But we need to define those needs, and then we need to determine the most efficient method of meeting those needs. Whether that means the Navy will design and maintain a fleet totally, or design and lease a fleet, or simply try to convert commercial vessels, needs to be determined.

I think the important point is that if these are U.S. national defense needs, the cost of these needs should not be borne by a specific segment of our economy, i.e., shippers. They should be borne generally by the U.S. taxpayer. And I think that if they are legitimate needs, then they will fairly be borne, and the U.S. taxpayer would agree to bear those costs.

PANEL ON ALTERNATIVE APPROACHES TO CARGO POLICY

December 4, 1984

PANELISTS

H. Clayton Cook
Cadwalader, Wickersham and Taft

Ernst Frankel
Massachusetts Institute of Technology

Leslie Kanuk
Baruch College

Harlan Ullman
Georgetown University

John Leeper
Simat, Inc.

TOPICS FOR DISCUSSION

1. Outlook for maritime industry and U.S. trade under current regulations, and potential benefits of changes in U.S. cargo-preference laws.
2. Developments in other countries' cargo policies and potential impacts on U.S. interests.
3. Possible response to future multilateral cargo policy initiatives and strategies to benefit U.S. interests.
4. Prospects for developing bilateral agreements, either in response to other nations' initiatives or as a U.S. initiative.
5. Outlook for changes in U.S. maritime industry prospects due to shifts U.S. or international cargo policies.

SUMMARY OF DISCUSSION

The panel on alternative approaches to cargo policy, which led off the second day of the OTA Workshop, was made up of participants with no direct interest in the maritime industry — academicians, consultants, etc. Because of this, they were asked to do a bit of "free thinking" and to develop possible alternative cargo policies.

Competition

A recurring theme was the need to develop a fully competitive atmosphere, in which shippers would have the freedom to choose among carriers in order to get the best combination of rates and service. At the same time, carriers would be protected. One way to achieve this would be the establishment of bilateral (or multilateral) shipping agreements, under which the national-flag carriers would compete for the available

business and other carriers would be excluded. There would be no conferences, no rate fixing, and no antitrust immunity. There would be complete freedom of entry into a trade. There would be no operating restrictions, such as now exist under operating differential subsidy regulations. There could be tax incentives for shippers to use U.S.-flag vessels. The Maritime Administration would continue to exist as a promotional agency, but all regulatory functions would be vested in an intergovernmental commission, which would adjudicate allegations of price fixing, discrimination, etc.[26]

Regulation

Overall, the panel agreed that a major problem facing the maritime industry today is over-regulation by the Government. There was general agreement that the Government's function should be only to set up a "protective cocoon" to deal with discriminatory practices by other countries, and then to assure free competition among carriers in a trade. It was stressed again and again that market forces must be allowed to govern.

Cargo Reservation

Another, but similar approach — multilateral cargo reservation, perhaps like that under the UNCTAD Liner Code — was put forth as essential to the security of the United States and its NATO allies. It was pointed out that not one West European or Scandinavian liner carrier is currently making enough money to allow replacement of its fleet. The outlook for availability of allied merchant vessels in support of a NATO in a future war is very gloomy. The reason for their depressed condition is that the Soviet Union is setting rates for its ships in these trades at 20 to 40 percent below conference rates. It is difficult for European countries to close their ports unilaterally because the Soviet Union is so near and is such an economic presence. Only through agreement between the United States and its free world allies can the fleets of our allies (and of the United States as well, when Soviet ships return to U.S. trades in great numbers) be assured a fair marketplace. If the United States took the lead, it could fashion a "limited flag" environment where competition could be maintained between certain registries, but controlled carriers could be prevented from destroying free world merchant fleets.[27]

On the actual UNCTAD Liner Code question, the panel called for U.S. leadership in solving restrictions on trade. Many countries that are signatories to the Liner Code (and

---

26. See the presentation by Leslie Kanuk, below.
27. See the presentation by Clayton Cook, below.

this may shortly include many of our major allies) are not anxious for restrictive cargo carriage. Some are in fact looking for loopholes to escape the full impact of the Liner Code. The United States must take an active and aggressive role in the international arena, both for national security and for commercial reasons.

Defense-Related Issues

The importance of the merchant fleet to national security was emphasized by panel members. At the same time, the Center for Strategic and International Studies has forecast that the U.S. maritime industry will decline by one-third or more by 1989.[28] The panel called for a comprehensive framework for both national security and commercial objectives. One element may be separating Government programs supporting shipyards from those supporting the operating industry. This point was raised a number of times throughout the sessions. Heavy manufacturing industry, like shipbuilding, is very different from transportation; solutions to their respective problems will be different as well.

Policy Needs

The need for flexibility in maritime policy was cited many times. The fact that the Merchant Marine Act of 1936 remained in place long after its usefulness had ended was responsible in part for the decline of the Merchant Marine. Through World War II, the Act accomplished its mission of building a U.S. merchant fleet. At that time, the United States had 61 percent of the world's tonnage. But continuing to subsidize a large healthy merchant marine during a time of limited competition resulted in a dependent and noncompetitive industry. The proliferation of Government restrictions and the disincentives to efficiency created by the subsidy system helped to undermine the fleet. Future policies must be structured more flexibility, so they can respond rapidly to the changing maritime environment.

Overall, the sense of this panel, as with several others, was that cargo policy should be an integral element of maritime policy, but in practice it should be used to increase marketplace freedom and competition. Unilateral commercial cargo reservation is detrimental to economic efficiency. Bilateral and multilateral agreements may be beneficial if they are structured so as to protect carriers against unfair trading practices and allow maximum market freedom within their framework.

---

28. See the presentation by Harlan Ullman, below.

Future Developments

This market freedom will allow innovative companies to flourish, while others may fail. The potential for growth in intermodalism was mentioned as an example. Some ports, like that of Seattle, are purchasing railroad cars and will offer their own intermodal service. The fact that some old-line maritime firms may be unable to compete with the innovators was seen as inevitable. The industry as a whole will be stronger and more competitive if innovation is more widespread.

PANELISTS' PRESENTATIONS

Leslie Kanuk, "Competition in a Protected Environment"[29]

As a former commissioner and former chairman of the Federal Maritime Commission, I come from a flag-blind environment. While on the Commission, I upheld the principle of flag-blindedness to the best of my ability. But viewing world shipping policies over the past few years, I have become convinced that U.S. policy initiatives must support U.S. interests. And these interests include not only shipper interests, but carrier interests and the national interest.

In the long term, I am convinced that shippers, carriers, and the general public all would benefit from a strong, competitive, and dependable U.S. merchant marine. The problem is how to get there, and still meet carrier and shipper short term needs.

And therein lies the paradox.

I think shippers — and through them the general public — would benefit from increased competition, in terms of rates, services, innovation, and so on. Our merchant marine, on the other hand, would benefit from bilateral treaties which reserve cargo by dividing up the trade, and thus severely restrict competition.

The challenge, then, is to find a way for competition to flourish in a protected environment — a seeming contradiction in terms. Yesterday we heard a number of positive and negative assessments of previous cargo policies, including a discussion of bilateral cargo policies. To my way of thinking, the most harmful, restrictive aspect of bilateral treaties is the allocation of fixed shares to national flags and to specific carriers. With guaranteed cargo shares, carriers do not have to outperform their competitiors to get cargo. They don't even have to try. In fact, most bilaterals are

---

29. Baruch College.

implemented through pools, which assess an overcarriage penalty to carriers who carry more than their allotted share. This encourages pool members to be undercarriers — that is, to perform so minimally that shippers will choose their competitors over them. Thus pools are the very antithesis of competition. That's what I found so insidious about pools in general, and that's why I was surprised at their inclusion in the 1984 Shipping Act. But let's get back to an effort to reconcile the short-term needs of shippers and carriers: to find a way for competition to operate in a protected environment. What I think is needed is some creative brainstorming from a group such as this.

Let me begin this process by presenting a straw man: a wild scenario in which competition would coexist with bilateralism. The purpose of this exercise is to serve as a basis for futher discussion, so I hope you will use it as a takeoff point.

Suppose the United States were to negotiate bilateral treaties with other nations, treaties which specifically ban the allocation of fixed shares. Then each national-flag carrier would have to compete with all the other carriers in the trade for market share. In order to operate in the trade, a carrier would have to be at least 50 percent owned by nationals of either trading partner. (This would permit a policy option of allowing ownership, rather than flag registry, to dictate participation in the trade.) Under this scenario, third flags would be excluded. Conferences, as we know them, would be banned, and every carrier would be an independent. There would be no rate fixing. One hundred percent of the trade would be a fair target for each carrier and for each trading partner. Thus, competition would flourish. This would require complete freedom of entry for legitimate national-flag carriers into the trade. MarAd would have to ease the acquisition of construction loans to facilitate entry to new U.S. carriers. Cross-chartering would be permitted at specially listed tariff rates, so that overtonnaging could be minimized. This would not require an agreement between carriers, but would simply be a form of buying space "wholesale."

To enable our carriers to really compete, we would have to free them from such operational constraints as they long endured under operational subsidy, such as essential trade route requirements, minimum or maximum sailing requirements, "build American" and "repair American" requirements. The support of our shipyards as a defense mobilization base would cease to be a burden placed on our carriers, but would more properly become the responsibility of the Department of Defense. Remember, the objective of this scenario is to increase competition — fair competition — within the framework of a bilateral treaty. If overtonnaging occurs and carriers fail as a result, then others will spring up. That's what competition is all about.

Each bilateral treaty would have to include the establishment of an intergovernmental committee to oversee the trade, to prohibit rate fixing, discrimination, etc. Both nations would be equally represented on such a committee, which would in essence be the regulatory agency that would oversee the trade to ensure that it operated fairly and in the public interest. There would be no granting of antitrust immunity, since all carriers would operate as independents. MarAd would continue to operate as a promotional agency for our merchant marine, and would preside over disputes which solely involve U.S. interests. Other disputes would be handled by the intergovernmental committee.

Under this scenario, some U.S. carriers may lose out; indeed, it is highly possible that U.S. carriers in a particular trade might aggregate far less than 50 percent of the trade. But it seems equally valid to assume that if we lose on some trade routes, we would gain on others. On balance, given our strength, our resources, and our know-how, the U.S. merchant fleet should come out ahead. Of course, the United States would have to educate American shippers on the need to support U.S. carriers. Tax incentives to "Ship American" might be in order. MarAd would have to be encouraged to develop more creative promotional strategies to benefit our carriers, while protecting the interests of our shippers.

As I said before, this is a rather wild scenario. But just possibly it could serve as a point of departure to trigger other, more pragmatic solutions to our very real maritime problems, solutions which would enable both shippers *and* carriers to benefit from new U.S. cargo policies.

H. Clayton Cook, "Cargo and Investment: Capital Formation in the United States Maritime Industry"[30]

It is a pleasure and a privilege to be here with you today. As General Counsel of the Maritime Administration I participated in government-to-government negotiations on behalf of the United States with the Soviet Union, with direct responsibility for the liner cargo-sharing provisions which that now expired agreement contained. As a practicing attorney, I have in recent years devoted the majority of my time to the legal and economic problems faced by a variety of maritime industry clients. In the course of this work, I have become familiar with the provisions of the UNCTAD Liner Code, its potential impact upon liner trades, and the complete absence of a coherent and realistic United States maritime policy — an absence noted both by the Office of Technology

30. Cadwalader, Wickersham, and Taft; extension of remarks presented at workshop.

Assessment in its October 1983 report and again by the Congressional Budget Office in its report of August 1984.

Much of what I will have to say here this morning will be unpopular with the Administration witnesses who have proceeded me on this panel. My analysis will, however, I am confident, find general favor within the liner shipping industry, in the United States and in Europe and the Far East, among both OECD and developing countries. It will also find approval among students of economics, and Government officials who have made the effort necessary to gain an understanding of the complexities of liner shipping in the container age — and the realities of our present world situation.

Introduction. — I would start with the proposition of Peter Douglas that ocean shippers should pay a fair rate, such that ocean carriers can enjoy a reasonable expectation of a return on capital invested:

> [A]cross the whole spectrum of the shipping market . . . most assuredly including the liner trades — ocean transportation is being provided today not merely at less than its full cost, but at freight rates which barely cover fuel and labor expenses alone. The amount of capital invested in cargo-carrying ships is at least twice what it was 10 years ago and market interest rates are virtually double what they were in 1973, yet vessel earnings, after payment of direct running costs, add up to billions of dollars less per year than they did in 1973. . . . Shippers can afford to pay their full share of capital costs which must be met if a viable seaborne cargo transport system is to be preserved for their continued use.[31]

I would posit to you that over the recent past, in the liner trades and in the bulk trades, ocean carriage has been subsidized by the owners of the ships involved, in many cases by massive government intervention, and in the instance of the Soviet bloc, by a system with rules and objectives which are so different from our own that it is improper to speak in terms of "subsidy" but rather in terms of "economic warfare." This situation, if allowed to continue, will result in a massive diminution in the liner trades of the Western and other OECD owners of the magnitude of the diminution in the bulk trade fleets described by yesterday afternoon's panelist.

Background. — Coming back from six weeks in Europe in August and September, where I spoke with senior shipping executives of most of the major Western European and Scandinavian carriers, I can fairly characterize the situation as one where probably not a single Western European or Scandinavian liner carrier is making profits sufficient to continue in the liner business. I do not mean by that, that an examination of the finan-

---

31. Peter S. Douglas, Chase Manhattan Bank N.A. (London), "Let's focus on freight rates!," *Seatrade*, February 1984, p. 112.

cial statement of every Western carrier for the current year will disclose losses. I do mean that Western carriers are operating in an environment where they are not making profits sufficient for fleet renewal, and in many cases there are actual losses.

If we look to Sweden, we see Brostrom's, once one of the great names in Western shipping, in bankruptcy. We see its assets transferred to Trans-
Atlantic and then read the announcement by Trans-Atlantic of projected losses for the current year that are the largest in its history. And we see Johnson Lines with losses in its operations, sustained only because it is a part of the Axel Johnson group.

We are faced with a situation where the pool of ships that our Defense Department planning looks to for NATO resupply, the ships of our NATO allies, is shrinking month by month. The official position of the Department of Transportation, the Department of State, and the Federal Maritime Commission, as reflected in numerous private conversations, and in the statements presented by their representatives at [OTA's] two-day cargo policy workshop, is that we must have "free competition" at all cost; that the failure of the Western European lines is an issue that Administration need not address; and that "free competition" is more important than the survival of Western European and other market-economy carriers.

An understanding of the Western maritime policy dilemma and its solution, and of alternative national cargo policies, requires some appreciation of recent history, of basic liner ship economics, and of the UNCTAD Liner Code. While, ideally, one might begin with the origins of the Liner Conference System in the 19th Century, the constraints of this forum will limit my review to the events of the last 20 years.

Soviet Expansion in the Decade of the 1970's. — The decade of the 1970's provided a continuation of Soviet actions of the 1960's, with an expanded Soviet fleet in the world's liner trades. The patterns of behavior were the same. Where the Soviets operated as outsiders, shippers were offered services at 20 to 50 percent below conference rates on selected highly rated cargoes. Generally, such rates were below the costs of OECD operators, and negotiations would be initiated in an attempt to reach some accommodation with the Soviet carrier involved.

Sometimes this would lead to admission into the conference. In this event, the Soviets generally asserted that their tonnage was inferior to that of the OECD carriers, and that the Soviet lines should accordingly be allowed conference status but special lower rates, most frequently 10 percent below those of other conference carriers, leaving the Soviets in a continuing preferred position with respect to conference shippers. Other

stratagems were used as well, all with the objective of increasing the Soviet share of conference carriage at the expense of the existing conference members.

In other instances the conferences resisted Soviet pressure, or the Soviet lines chose not to seek conference entry. These situations were generally characterized by negotiations between OECD shipowner associations and the Soviet lines involved. A typical progression involved the Soviets first pleading that their situation was atypical and their rates fair. Then, after a period of time during which the Soviets continued to expand their presence, some agreement as to limitations of additional tonnage and sailings would be reached. In the majority of cases, these agreements were not effective because, as we understand the use of words in the West, they were not honored. Typically there were Soviet assertions that the agreement had not covered the specific point involved, or that there had been a change in circumstances allowing a change in Soviet position.

The measure of difficulties became more apparent as the decade progressed. During the period 1969 through 1979 the Soviets had increased the number of ships in service from 5,622 to 8,120, with a companion increase in gross tonnage from 13.7 million to 22.9 million gross tons.

Significant inroads in what had traditionally been OECD shipping were achieved by means of selective or general tariff reductions by the Soviet cross-traders, supported by a worldwide network of Soviet-controlled or Soviet-affiliated shipping and forwarding agencies. For the first time many conference carriers recognized that while they had dealt with independent outsider competition before, they now faced an entirely different challenge — "competition" with state-owned, government-controlled systems, with the entire financial backing and resources of the Soviet state, which would enable the "independent" line to remain in the trade indefinitely, and entirely without regard to market profitability concerns.

The difficulties caused by Soviet cross-trading lead to a number of critical situations in the OECD liner trades. The effect of Soviet penetration was not limited to the revenue loss associated with the specific cargo lost, but included as well the revenues foregone as the result of Western carriers' rate reductions in attempts to meet Soviet "competition." The lowering of rates in order to preserve vital markets left many OECD operators with limited margins of operating profit, significantly affecting their long-term financial structure and their ability to engage in needed fleet modernization — quite apart from fleet enhancement or growth. In certain liner services the Soviet "competition" proved so serious as to cause substantial rationalizations, consolidations, closures, and bankruptcies for the affected Western carriers.

Soviet Expansion in the Decade of the 1980's. — As the 1980's began, the potential effects of Soviet economic warfare became more clearly visible. In the always carefully phrased words of the OECD Maritime Transport Committee:

> In the future . . . the projected growth in overall [Soviet] cargo capacity may become a real danger, particularly the introduction of part and full containership and roll-on/roll-off vessels of high flexibility, which could . . . cause a significant reduction in the participation of OECD transport services in bilateral and international seaborne trade so that USSR shipping could well attain a very substantial position in many world trades. . . . In the state trading sector, the basic problem is the lack of reciprocity between the two sides, and the inherent incompatibility of the two economic systems which leads to a *"dialogue de sourds"* [among the deaf].

At the end of 1983 the Committee would state that for that year:

> [I]n spite of assurances given at a political level during the 1982-83 bilateral and multilateral discussions with OECD Member government, the USSR did not d how any real willingness to reach an equitable commercial compromise. By mid-1983, 243 vessels, with a total of 2.17 million dwt, were engaged in about 51 main liner trades. Compared with mid-1982 there was no substantial change in the total tonnage utilized, but a constant improvement in its quality could be observed. The Soviets maintained their strong position with aggressive rating policies, in particular in the Far East trades. They indicated some willingness to conclude arrangements in the Europe-Central American trades, but continued to show intransigence in the East African trades, although an agreement could have been reached in that area.

Looking to the future, it was the Committee's conclusion that with respect to the Soviets:

> In spite of all moves from the Western side to find arrangements with the Soviets acceptable to all parties, it must regretfully be stated that the Soviets appear to have failed to comply with the undertakings they agreed to in January 1982. Soviet lines . . . by their trading and rate cutting practices have continued their penetration into liner conference trade routes in order to pursue political and economic objectives.

The Committee concluded that for the foreseeable future, OECD shipowners in conference liner shipping could expect rates which would barely cover the *operating* costs of the most efficient companies, and would endanger the commercial viability of a substantial number of OECD shipowners, conclusions which were and are today widely shared.

Pondering the above, one can do no better than to consider the recent statement by Hans Jakob Kruse, Chairman of Hapag-Lloyd AG, to the effect that: "Time is running out for all Western European governments if the trend of shrinkage of their merchant marines is not to become irrevocable, with all its far reaching political and strategical consequences." The Soviet position is clear:

> [T]he development and use of merchant fleets of various countries in peacetime are . . . [part] of that economic and political struggle in the

international arena which continues to remain an unchanged accompaniment of antagonistic social systems.

Under present circumstances, the prerequisite for OECD carrier survival will not be carrier efficiency, but rather the degree of government support that OECD carriers will enjoy.

The United States Experience 1972-1981. — With U.S. ports effectively closed to Soviet shipping prior to 1972, under rules which denied Soviet vessel access except upon 14 days advance request, U.S. shipowners were insulated from the Soviet problems suffered by their Western European and Japanese counterparts.

Negotiations concerning the Maritime agreement between the United States and the Soviet Union, signed in October 1972, were from the U.S. standpoint focused principally on the bulk trade provisions. These were reviewed as of primary importance in connection with the U.S. grain sales, which provided the basic motivation for an agreement on port access and cargo sharing. But clearly the Soviet negotiators had as a principal objective, entry of their liner vessels into the ports of the world's principal trading nation and their stated "main adversary."

As a result of the accord, Soviet Mortlot liner vessels promptly entered the U.S. cross-trades. In the North Atlantic and North Pacific they quoted rates designed to attract the more highly rated cargoes, creating market chaos and leaving the free market economy lines of the United States and our OECD allies with diminishing cargo shares. In the decade that followed, the Soviet lines succeeded in capturing approximately 13 percent of the liner cargoes between the United States and Western Europe, carrying in excess of 25 percent of the traffic between the Federal Republic of Germany and the United States. In the U.S.-Far East trades, the Soviet Far East Shipping Company (FESCO), quoting rates 26 to 38 percent lower than conference members, rose to clearly dominate the field of 24 competing firms, with a 23-percent lead in sales volume over its nearest competitor. Among the resulting casualties were two U.S. carriers, Pacific Far East Line and States Steamship Lines, which were forced into bankruptcy. The revenues accruing to the Soviets from the lucrative U.S. trades were expected to finance further Soviet fleet additions, and access to U.S. ports would provide a helpful stepping stone for the penetration of South American trades.

With the reimposition of the International Longshoreman's Association refusal to handle Soviet vessel cargoes as the result of Soviet actions in Afghanistan, and faced with general public and shipper hostility, the Soviets withdrew from the Imoted States operations in 1980. While negotiations were initiated for the renewal of the Maritime

Agreement (executed in 1975 as the successor to the 1972 Agreement), the 1975 Agreement was allowed to expire in accordance with its terms on December 31, 1981. Today Soviet Block cross-trading of U.S. cargoes continues on a much reduced scale, limited to movements through Canadian ports and indirect service by Polish Ocean Lines.

As a result of the withdrawal of the Morflot fleets from U.S. service, the problems posed by Soviet cross-trading activities have, in the words of one senior Administration official charged with maritime policy matters, "largely receded from our consciousness." Recent discussions by West European shipowners and NATO government representatives, concerning U.S. support in a coordinated effort to oppose the challenge of Soviet practices; have met studied indifference at the Department of Transportation and the Department of State.

The UNCTAD Liner Code 1965-1983. — While successful in their program of "economic warfare," Soviet efforts in the United Nations Conference on Trade and Development (UNCTAD) were not nearly so fruitful. As a result of thoughtful research and expert drafting, the Code of Conduct for Liner Conference as finally presented for approval in 1974 represented a strongly pro-liner-conference document. It provided a balanced approach to established positions of the existing OECD carriers, to the problems and aspirations of developing countries, and to the needs and remedies of ocean shippers and ocean liner carriers — and it was clearly alien to Soviet objectives. Its objective was to "improve the liner conference system," and its goals and principles were:

1. orderly expansion of world seaborne trade;
2. development of regular and efficient liner services adequate to the requirements of the trade concerned;
3. a balance of interests between suppliers and users of liner shipping services;
4. nondiscrimination against shipowners, shippers, or the foreign trade of any country;
5. meaningful consultations between shippers and conferences, with, upon request, participation of appropriate authorities; and
6. conferences to provide suitable information on their activities.

Those voting in favor of adoption included all of the participating developing countries and seven OECD members. Other than Switzerland, the European countries that rejected adoption did so because of the cargo-reservation provisions, and attendant restrictions on cross-trading, which they believed were of potential harm to their fleets. The United States, however, voted against the Code on "free trade" principles, on

the basis that the cargo-sharing provisions, which would have benefited U.S.-flag vessel owners, violated long established policies and the existing precepts of anti-trust law.

The wording of the UNCTAD Liner Code is in some respects deliberately open. In its general form, it provides for a balancing of supply and demand through some form of service rationalization. Article 1, on membership, allows conferences. Article 2, on participation in trades, recognizes the desirability of allowing third-country carriage of up to 20 percent of the trade. Articles 1 and 2, together with Article 7, dealing with loyalty arrangements, provide authority for the full rationalization of services (including pooling agreements, deferred rebates, other contractual arrangements), so long as certain safeguards are observed for the protection of shippers.

It is perhaps one of the major ironies of the past two decades that the UNCTAD Liner Code, which provides an effective means of general applicability, with treaty authority and the approval of overwhelming majority of the shipowner and shipping nations of the world and which would have provided the means for countering the ever-expanding scope of Soviet economic warfare, was not promptly seized upon, ratified and implemented. It was not until October 1983, with the deposit of notice of the official ratifications of the Netherlands and the Federal Republic of Germany, that the UNCTAD Liner Code came into effect.

United States Maritime Policy and Reality. — U.S. maritime policy should be formulated and executed in a fashion designed to meet this Nation's needs — paramount among these, its national defense and security needs and those of its NATO and other allies. The basic legislative policy authority presently in effect in the Merchant Marine Act of 1936, specifically mandates that:

> *It is necessary for the national defense* . . . that the United States shall have a merchant marine . . . capable of serving as a naval and military auxiliary in time of war or national emergency . . . supplemented by efficient facilities for shipbuilding and ship repair.

Today, no longer possessing the geographic isolation that provided the time necessary to prepare our defenses in World Wars I and II, this U.S.-flag merchant fleet and associated shipyard facilities must be developed and sustained in time of peace if they are to be available in time of war.

Within the present Administration, there has been a stated recognition of this need by the President and by the Secretary of Defense. Yet the Department of Transportation has failed to formulate a plan to meet this need, because (like the Department of State) it has failed to deal with world liner shipping/shipbuilding, as they actually exist, rather than as these Departments wish them to be and it has failed to face economic realities,

rather than simply urging "free market competition" as the resolution to maritime problems.

The Present Situation: 1985. — Consistent with the U.S. military strategy of forward defense, about one-fourth of our land combat forces are stationed overseas and would require supply in the event of hostilities. The billions of dollars spent each year on general combat and support forces located in the United States are predicated on the assumption that these forces can be transported into combat abroad. Ships would carry some portions of these forces, and almost all of their equipment and other supplies. Ninety-five percent of dry bulk material and over 99 percent of all petroleum products needed to sustain an overseas war would have to be transported by sealift. Sealift is a fundamental part of the U.S. national defense posture.

The U.S.-flag liner fleet and the fleets of our NATO and other allies are well suited to meet military support needs in the event of hostilities. They are an essential element in current defense planning. Available unclassified studies suggest that existing U.S.-flag liner fleet capacity — that is, our combined Jones Act and foreign trade liner fleets — would probably be sufficient, together with the fleets of our NATO allies, to meet NATO initial resupply contingencies. These same studies, however, show that there is a serious shortfall of surge capacity tonnage, and of the tonnage necessary in any situation of horizontal escalation, or of prolonged hostilities in Eastern Mediterranean, East Asian, or other theaters requiring supply and resupply tonnage capability.

The need for a U.S. policy response to the precarious economic viability of the liner fleets of our Western European allies is underscored by the fact that there is probably not a single liner operating company from those countries generating sufficient revenues to provide for vessel replacement costs. The sizes of their flag fleets have declined dramatically. In 1982, the most recent year for which figures are available, Federal Republic-flag vessels carried only 12.9 percent of that nation's import trade and only 20 percent of its export trade. In the same year, British vessels carried only 29.2 percent of Great Britain's import trade and 27.1 percent of its export trade, while French ships carried 25.5 percent of France's import trade and 21.2 percent of its export trade. For the Netherlands, the figures for the same period were 2.2 percent and 8.7 percent.

In contrast to the fleet declines suffered by the United States and its NATO allies is the steady growth — and enhanced military adaptability — of the merchant fleet of the Soviet Union over the past two decades. The growth in the Soviet merchant fleet, in and of itself, is sobering. What is alarming, however, is that this growth has itself been the principal cause of the diminution in the size of the fleets of our NATO and OECD allies.

The present Administration is charged with the responsibility for implementing the 1936 Act and the maritime policy which it sets forth. It can do so by adopting the UNCTAD Liner Code, with appropriate national cargo-reservation policies in consultation with our allies, coupled with a preference for U.S.-built vessels in the carriage of cargo reserved for U.S.-flag carriage. Significant Federal budgetary savings could be expected in the adoption of such a policy.

The Basic Economic Frame of Reference. — The maintenance and enhancement of U.S., NATO, and OECD liner fleet capacity involves a number of factors. The basic economic framework may, however, be understood by an analysis limited to the Pacific, North Atlantic, and West Europe-Far East trades, which account for more than 70 percent of the world's liner trade volume. For 1985, the share of this trade attributable to OECD countries is approximately two-thirds of the total, with OECD-flag vessels constituting approximately 70 percent of available vessel capacity. The share of this trade attributable to Soviet Block countries is shown to be approximately 1.25 percent, with Soviet Bloc-flag vessels constituting 8 percent of available vessel capacity, or 6.5 times (650 percent) more than the amount of the cargo which the Soviet Bloc countries generate. The Peoples Republic of China (PRC) has cargo capacity three times (300 percent) larger than its cargo contribution.

The disparity between cargo volume and overall fleet capacity, as projected for 1985, is such that capacity will be approximately 1.5 times (150 percent) more than the cargo volume. The expected result of this overcapacity will be rate reductions by Soviet carriers to levels that are below OECD carrier costs, but which the Soviet Block and PRC carriers, and perhaps the Taiwanese carriers, can sustain. As rates are reduced, these countries' fleets will obtain increasingly larger shares of the cargo generated by the OECD countries in these trades; this will in turn produce OECD liner company bankruptcies and further reductions in NATO available tonnage.

Conclusion: A Maritime Policy Response. — A solution to this problem is available in the adoption by the United States of the UNCTAD Liner Code, accompanied by appropriate enabling legislation which would come into effect promptly after enactment. Such legislation would provide for reservation of *all* liner cargoes, and the sharing of cargoes equally by the Government-designated "national shipping lines," and those of our trading partners and cross-traders, on the 40-40-20 percent basis suggested by Article 2 of the UNCTAD Liner Code. This would be coupled with a preference for U.S.-built vessels in the carriage of the U.S. reserved share.

Adoption of the UNCTAD Liner Code would be the initial step in a comprehensive plan to meet U.S. national defense and national security maritime needs and those of our NATO and other allies, and to assist our developing trading partners in the development of their maritime capabilities. The adoption of the UNCTAD Liner Code on the above basis should allow the termination of all existing MarAd subsidy and aid programs, resulting in substantial budgetary savings.

U.S. export and import trades would not be harmed, but would in fact benefit. The added offsetting cost of a U.S. shipbuilding preference to a consumer-purchaser in the United States or abroad has been calculated to be in the range of 1 to 2 percent of the purchase price of goods. This cost would be more than offset by the rate reductions which could be expected as a consequence of the higher vessel utilization rates and higher shipowner profits which would result.

All of our OECD allies have either adopted or announced their intention to adopt the UNCTAD Liner Code in some form. The majority if not all of our NATO allies (Greece may be the only exception) would favor U.S. adoption of the UNCTAD Liner Code without the "Brussels Reservations," so long as access to our cross-trades was afforded their carriers. None of our NATO allies would object to the adoption of a preference for U.S.-built ships, though Japan's position on this issue is uncertain.

All of our Latin American allies, and most if not all developing countries other than those under Soviet domination, would favor U.S. adoption of the UNCTAD Liner Code on the basis outlined, with the possible exception of the PRC and Taiwan, whose future cross-trading activities might be curtailed, and Korea, whose sole objection would be that its shipbuilding industry would be affected.

U.S. adoption of the UNCTAD Liner Code on the basis outlined would provide the basis and encouragement for EEC modification or elimination of the "Brussels Reservations," which while originally designed to protect the cross-trading interests of the United Kingdom and Scandinavian shipowners are now, as the result of Soviet "competition," proving to be their undoing. Such a course of action, after consultation and if properly presented, would be welcomed throughout the free world as an act evidencing leadership and realism. And it would lay the groundwork for the preservation of the liner fleets of our OECD and developing trading partners, and the protection and development of their liner merchant fleets, consistent with true "free market" principles and with protection from Soviet "economic warfare."

Serious study of the adoption of the UNCTAD Liner Code has been prevented by Departments of State and Transportation on the basis that it is "anti-free-trade" and "anticompetitive." These Departments continue to urge solution of our maritime problems upon "free market commercial principles," while the Soviet Union is succeeding in a strategy of "economic warfare" designed to deny to the United States and our NATO allies the liner merchant fleets necessary to the maintenance of the alliance, and at the same time enhancing Soviet maritime support capabilities with vessels that are being paid for by the carriage of OECD and NATO country cargoes.

Thank you very much.

Ernst Frankel[32]

Thank you, Mr. Chairman. I appreciate the opportunity of commenting on some of the issues here.

I must admit that I expected a somewhat different format of the workshop because I thought that our task is to come up with novel ideas on cargo policies for consideration by the U.S. Congress.

Instead, I listened with great interest yesterday to the deliberations of the three panels, and couldn't help to think that it is all *deja vu* — these are arguments, parochial arguments, which have been expounded over and over again. Apparently no sector, however minute, of the maritime industry has been willing to consider the interests of the other sectors or of the nation as a whole.

In fact, I believe — and it may make me rather unpopular in this surrounding, but being an academic I can usually afford this — that our maritime industry is today probably more divided than it has ever been before. The various sectors of the industry are holding out for their particular interests and want to make sure that their interests are taken care of and are considered independent of the overall good of the nation, the industry, so on and so forth.

On the other hand, in work with some of the major international organizations in recent years, most recently in Geneva at the UNCTAD conference, I have the distinct feeling that the rest of the world, and particularly the other OECD nations and a significant proportion of the LDC nations, are waiting for some form of leadership from us, some maritime policies, some pronouncements of where things ought to go.

---

32. Massachusetts Institute of Technology.

In fact, there are clear indications that the long delay in enactment of the Code [occurred because other nations have] been waiting for the United States to act, to take some position. In fact, my feeling is that we have [followed] an ostrich policy — we buried our head in the sand and just ignored or refused to consider it in any form whatsoever.

It is true that certain aspects of the Code are contrary to U.S. law and to our concept of free trade and free competition, but then again we all know — and we heard yesterday that we were among the [leaders] in [this] — sometimes we are dragged into bilateral shipping agreements and other restrictive practices. Therefore, many of our friends abroad are asking the valid question: why weren't you willing to discuss amendments or changes, or discuss the Code *per se* in more detail, and consider formulating it differently in a way that you, as the leader in world trade, could accept it?

We have heard many [examples] in the last two days of the various impacts that cargo policies would have on the various sectors of the maritime industry, including obviously shippers and producers like the Farm Bureau. On the other hand, I have not heard any consensus on the basic interests that we should all share. This is quite contrary to developments in some other countries. The Japanese, for example, or some of our other OECD friends, have been able to get together and — though their maritime industry is probably as divided as ours, and certainly has many diverse interests in it — they have been able to come to some terms and allow their respective governments and representatives to agree to some common basis.

I listened with great interest to Dr. Kanuk's wild scenario, and I don't think it's wild at all. I think the time has come for us to step back; to forget what we have done for the last 70 or nearly 70 years since the Shipping Act of 1916, which has been amended and amended and amended, over and over again; [to stop] assuming that the [conditions] that led to the Shipping Act of 1916 still exist in 1984; and [instead to] look at the world the way it is, the role we play in the world, the role our maritime trade and maritime industry ought to play.

There are some very basic and simple issues which, in my opinion, have to be resolved first of all. In all the discussions here and abroad on maritime policy and cargo policy in particular, the first problem I face is semantics. We talk of national shipping, we talk of legislation, we call for controlled cargoes — and if, after a meeting, when many speakers address those topics, you sit around a dinner table or a bar table and try to find out what exactly did each imply by these terms, you find that there are as many opinions as there are participants in the discussion.

I believe we need a much more explicit definition of what we mean by these terms. And by my recent visit to Geneva, I found that even the participants at the UNCTAD conference are as diverse in their interpretation of these terms as I thought they would be.

This even applies to such things as Government-impelled or Government-controlled cargoes, for example. We recently sent questionnaires to 26 governments to try to find out what they mean by it, and we got 26 different answers which apply to different types of cargoes, different control, different ownership. It doesn't mean any one thing.

So I believe we really have to go back to the baseline and try to define what we are talking about, what the terms that we use in all our deliberations really mean.

Now, I agree with most of the comments on the scenario presented by Dr. Kanuk. I think it's not only very imaginative, I think it's also quite realistic. I would like to expand this to multilateral trade, because one of the problems with bilateral agreements, open or closed — with open competition, as Dr. Kanuk so well described — is the disadvantage of a less-than-effective utilization of resources, because very few bilateral trades are effectively balanced and cost rates are required both in liner and in bulk trades to make effective use of capacity.

Again, one of the problems we face in this area is that while we discuss policy and propose policy changes, in most cases that I am aware of we haven't really done our homework. We don't really know or have not studied the potential implications of those policy changes. We don't know what economic or operational issues would be affected by such policy changes, if implemented.

In fact, I am surprised at the amount of effort we usually put into discussing policy and how little effort is put into studying the various scenarios, implications of policy changes in economic and operational terms. Now, the panel on alternative cargo policies was supposed to address five major issues — and I am afraid I shouldn't take your time in discussing some of the comments that I noted down — but if I address them in terms of the outlook for maritime industry under current regulations and benefits of changes in U.S. cargo preference laws — well, I think frankly that major changes are required before we get a more positive outlook in the maritime industry.

Now, one thing we should also consider is that, although we initially opposed the Liner Code of Conduct and obviously oppose similar approaches towards restrictive practices in the bulk trade, the large majority of nations who have ratified the Liner Code of Conduct don't really apply it. In fact, they are looking for all kinds of loopholes

and reinterpretations, because they have found by and large that the rigid application of the terms of the Code, not only with regard to cargo shares but also with regard to other terms of the Code, are economically disastrous.

Here again, many of these nations are looking to us for some kind of leadership. Most of them do not have the capability of studying the economic and operational implications. They don't really know why certain things don't work, but they know that things have become more expensive. The example quoted yesterday of the higher cost of liner shipping in the U.S.-Argentine-Brazilian trade under bilateral trading agreements, has been repeated in many other cases. Some countries in southeast Asia have recently made studies of the implications of shipping restrictions for the cost of trade, and they have come to similar conclusions.

Let me therefore conclude, because I am afraid my time is probably up, that I believe we have to develop more imaginative cargo policies. Examples such as the scenario presented by Dr. Kanuk are not wild; I think they ought to be taken very seriously. There are many variations on that theme. I have a similar but somewhat diverse proposal for multilateral cargo policy, which would include conference participation — but I don't think we have enough time to discuss this in detail.

Let me, therefore, simply say that I believe the time has come for us to take the issue more seriously, do our homework, come up with more imaginative cargo policies, and put many of our parochial interests in the background. We must look at the overall picture, and then try to meet the parochical interests as part of meeting the overall objectives.

Harlan Ullman[33]

Mr. Chairman, ladies and gentlemen, good morning. I am Harlan Ullman of the Center for Strategic and International Studies [CSIS] at Georgetown University.

To begin my remarks I would like to invoke two names which are not normally found in this particular committee room, nor indeed with maritime affairs — Samuel Johnson and Sigmund Freud — because a lot of what I am going to say dwells heavily on [how] the prospect of being hanged in the morning [helps in] clearing one's head, and then questioning how in the first place we ever got ourselves in this position.

---

33. Center for Strategic and International Studies, Georgetown University.

To that end I would like to make four points. The first point has to do with forecasts for the future aggregate levels of U.S. commercial maritime industries. In reviewing what the forecasts are, I am reminded of an observation made many years ago, when the Greeks were still in the maritime business, by a good friend who was then and still is chief of Niarchos's European operations. He noted rather cynically that the only guaranteed way to make a small fortune in the maritime area was to start with a large one. And, unfortunately, that is perhaps altogether too true today.

In terms of our forecast for U.S. maritime industries — that is, U.S.-flag fleet and U.S. private shipyards — we estimate that by 1989 there will be a total decline of at least a third or more in aggregate terms. I won't go into the specifics, because trading off tons and hulls and numbers — those units are not exactly fungible. The details will be forthcoming in a publication that we hope to get out this Friday, though we have some draft copies here.

But if that in fact is true and if our analysis is reasonably correct, as we think it is, how did we get ourselves in this situation? Why is this not more widely known beyond just those people with interests in the maritime industry? After all, this Nation has long been reliant on the seas.

This gets me to my second point, which has to do with the psychology, the culture, and the social structure of the American people. We are largely optimistic, we like to believe that we solve problems, but we are not prepared to address every problem. One example will suffice.

For the past 30 or 35 years we have spent approximately 20 percent, or thereabouts, of our defense budget on the procuring and operations of nuclear weapons. We have now, by a given count, perhaps 10,000 to 12,000 strategic nuclear warheads in our arsenal. The Russians have about the same. Yet when we get to the stage where our policymakers and not technicians begin to wonder what if those weapons have to be used, it becomes almost impossible to join a public debate, because the prospects are either too frightening or too destabilizing. So, therefore, in an issue of fundamental national security import, nuclear weapons, we are often limited in serious discussions.

Whereas I do not mean to combine the maritime industries with nuclear weapons, let me say that this issue in its own way, may be as important to the well-being of this country. [And yet] we find it extremely difficult to join a serious and widespread debate about whether or not this forecasted decline is or is not in the national interest, and whether or not we ought to do something about it.

This gets me to another question, which is what shall we do about all this? Now, I disagree with those who say we don't need more comprehensive analyses. To the degree that we don't need any new studies, I am in full agreement; there certainly have been more than enough studies. But what has not been done, in my mind, in a satisfactory way at all is to combine comprehensively a framework for addressing these critical issues that join national security, national defense, and the direct and indirect costs and benefits of maintaining U.S. maritime industries, both shipbuilding and shipping lines.

Take, for example, the issue of cargo preference. Now, depending upon where you look and to whom you talk, you can find that cargo-preference laws, or increases in cargo-preference shares, may cost the American taxpayer very, very little, or that they may cost as much as $1 billion to $2 billion a year. Let's assume, for argument's sake — and I am not saying this figure is right or wrong — that it will cost about a billion dollars a year to maintain cargo preferences, which will then be plowed back to the respective industries.

Now, nowhere have we really looked in terms of tradeoffs, what that billion dollars might get us if it was being spent elsewhere or whether it was being spent in terms of supporting the maritime industries. A billion dollars of farm subsidies, tax credits, dare I say, in terms of the Department of Defense — these kinds of aggregate tradeoffs, it seems to me, need to be examined. That has not really been done in a comprehensive fashion, and therefore it's very difficult, not only in terms of disseminating the issues surrounding the maritime industries, but also in terms of coming up with what could be called sensible maritime policies.

This gets me to my third point. I would suggest that one thing that needs to be done is to take a very serious look at separating, or at least seeing the costs and benefits of separating, the notion of shipyards from [that of] U.S.-flag fleet shipping industries. Now, they have been joined since 1936 on the notion of subsidies. Clearly there are links beyond just the similar first name of "ship." But it seems to me that if we are at a stage where there are distinct differences between heavy industry (as dealing with shipyards) and transportation (as dealing with shipping in general), then perhaps there have got to be alternate solutions. Now, those solutions may be linked, but it seems to me that it may be unwise to try and proceed with policies that are designed to solve both sets of issues, when in fact those policies may be contradictory. And I think that deserves very serious attention.

To that end, we are in the process of putting together a maritime options paper which will build on the forecast.[34] We will take a look in the broadest sense at what alternative maritime policies may be and what the cost-benefits of them might also be. This is not in terms of an advocacy, but rather as a straightforward cost-benefit analysis, because CSIS, to the best of my knowledge, owns no shipyards nor ships and isn't intending to get into that business. We feel that the public debate needs to be joined and a comprehensive framework is needed for examining the full range of issues with a cost-benefit analysis.

Let me conclude by saying that it seems to us that 1985 should be a year of deliberation, dissemination, and decision concerning U.S. maritime capabilities. The Commission on the Merchant Marine and the National Defense is indeed an excellent vehicle by which some of the problems in the U.S. maritime industries can be further publicized. It is our view that expanding and broadening public debate, making aware what the forecasts and implications of the maritime industries' future happen to be, and then raising the questions of whether or not that decline is or is not in the national interest, is something that needs to be done.

Mr. Chairman, we are working to that end, and I hope by the middle of next year we will come up with an options paper which raises the issues and answers some of these questions that I have put today. Thank you.

John Leeper, "Cargo Policy, The Ultimate Solution?"[35]

For over 200 years, the United States has been searching for an enduring industrial strategy for its merchant marine. The result of this seemingly unending quest might best be summarized by following excerpts, which characterize the state of the merchant marine industry today:

> American vessels in foreign trade may be divided into two classes: those able to operate without Government assistance and those which require subsidies.
>
> * * *
>
> Careful examination of the arguments advanced in behalf of an American merchant marine indicates that there are only two sound considerations that justify the expenditure of public funds to maintain a foreign-going fleet by the United States. One of these considerations is the importance of shipping as a factor in the preservation and development of foreign commerce; the other is the relationship that exists between merchant vessels and national defense.

---

34. "Forecasts for U.S. Maritime Industries in 1989," by Harlan Ullman and Paula Pettavino, CSIS Significant Issues Series, vol. VI, No. 17, December 1984.

* * *

Careful study of all possible contingencies indicates that the military forces would require, in the event of war with a major power, a minimum of 1,000 merchant ships of all types, aggregating about 6 million gross tons.

* * *

Measured by any of the usual standards, such as capitalization, revenues, and employment, the subsidized merchant marine is revealed as a surprisingly small industry.

* * *

Analysis of the financial condition of the subsidized lines, in view of the replacement needs of the companies, reveals a truly depressing outlook for this segment of the industry. Some of the lines appear to be in good shape; the condition of others is dubious; some apparently have little chance of survival.

* * *

A weakness of the American merchant marine, and one which seems unlikely to be remedied in the near future, is the hesitancy of private capital with regard to this industry.

* * *

The unattractiveness of shipping to the investor is not peculiar to this period; nor is it confined to American companies. Shipping has been, in the financial sense, a sick industry for many years.

* * *

The Commission believes that the requirements of trade, as revealed by a study of the individual routes, should be fully met. It believes, further, that the requirements of defense should be met. The Commission does not believe, however, that the requirements should be confused. Expenditures for commercial purposes should be so designated; any additional expense incurred for reasons of defense should be earmarked. *The people have a right to know just where their money goes.*

Are these clippings from last week's *American Shipper*? They could be, but in fact they were taken from a document published by the U.S. Maritime Commission in 1937, entitled *An Economic Survey of the American Merchant Marine.*

Since U.S. maritime industrial policy has been dominated by a single law (the Merchant Marine Act 1936) from the time the above statements were made until today, it would appear that almost 50 years of dollars and dedication have been wasted. The conditions the policy set out to correct are still with us. An enduring industrial policy seems to evade our grasp.

However, a closer and more thoughtful examination leads to a somewhat different conclusion. The Merchant Marine Act of 1936 was in fact a magnificent success in its time. It gave the U.S. a head start on World War II and enabled us to expand our merchant fleet from 1,400 vessels in 1938 to 5,500 in 1945. However, in my opinion, when the war ended in 1945, the Merchant Marine Act of 1936 should have been retired.

---

35. Simat International, Inc.

There was no need in 1945 to subsidize the world's largest merchant marine. As the war ended, our merchant vessels accounted for 61 percent of the world's surviving tonnage. Subsidizing a healthy merchant marine during a period of limited competition resulted in a dependent and competitively unresponsive industry. The problem with the Act of 1936 was not that it was poorly conceived, but that it was allowed to outlive its usefulness.

Can cargo policy replace the 1936 Act as our primary instrument of merchant marine promotion? Is cargo policy the ultimate solution? If there is an enduring maritime policy or ultimate answer, it is that our maritime industrial policy must be both flexible and precise. World political, social, and industrial conditions change, and our policies must change with them. Cargo policy alone is not the ultimate answer.

In reading some of the deliberations that led to the passage of 1936 Act, I came across the statement made in 1932 by the then President of the Propeller Club of the United States, who stated that the greatest problem facing the U.S. merchant marine was the Volstead Act, which of course was prohibition. He was referring to the difficulty U.S. passenger ships had in competing with foreign-flag ships that served liquor. This problem seems unreal to us today, but it was in fact a problem in 1932.

This brief journey into the history of U.S. merchant marine policy is, I believe, a necessary preamble to an evaluation of cargo policy alternatives. If we are to embrace cargo policy as a part of U.S. maritime industrial strategy, we must be sure that it addresses tomorrow's problems and that we can control its impact once it is unleashed on the world.

There are four cargo policy alternatives open to the U.S. today:

- unilateral reservation of commercial cargoes;
- unilateral reservation of non-commercial cargoes;
- selective bi-lateral agreements; or
- the UNCTAD Code.

The current U.S. cargo policy allows for the reservation of noncommercial military and AID cargoes and provides for the implementation of selective bilateral agreements. To date, the Administration has rejected unilateral cargo reservation and the UNCTAD Code.

Although the Administration's position on cargo policy has been criticized by many, it holds up under close analysis. Unilateral reservation of commercial cargoes is, in my opinion, not desirable from either a theoretical or a practical viewpoint. Selective bilateral agreements and the reservation of noncommercial cargoes are acceptable.

Theoretically, the reservation of commercial cargoes is a device that employs both protectionism and subsidy. As the world's largest trading nation, we must be careful not to initiate a chain of protectionist reactions around the world. Almost all economists agree that an international wave of protectionist legislation creating new tariff and nontariff barriers to trade would result in a massive worldwide recession. The life-blood of the merchant marine industries is world trade. Without world trade there is no need for ships or seamen or longshoremen. It seems to me that the long term position of the merchant marine industry has to be one of promoting world trade, on the theory that it is better to have a smaller share of growing market rather than a larger share of a declining on nonexistent market. While the United States may eventually end up negotiating a series of bilateral agreements that in effect create a cargo-reservation environment around the world, such agreements will be negotiated in a slow and deliberative method that will not create reactionary countermeasures among the world's traders.

Unilateral cargo reservation by the U.S. would send signals to our own domestic manufacturers that tariff and nontariff barriers to world trade are acceptable. Consumer products such as automobiles, electronics, and household items now make up nearly 20 percent of U.S. foreign trade. Tariff barriers would halt the inflow of these goods, and U.S. liner operators and U.S. seamen and longshoremen would suffer.

From a practical perspective, it is also *not* probable that the merchant marine industries could force unilateral cargo reservation through Congress and the President. The maritime community has demonstrated rather consistently that it does not have the political muscle to emerge victorious in even the smallest skirmishes within either the legislative or administrative branch of the Government. Even if there was unanimity within the maritime community, it would be difficult to overcome the opposition to cargo reservation that would be posed by a massive coalition of shippers, consumers, oil, and agriculture.

Agriculture's arguments against cargo reservation are particularly compelling. Agriculture is one of our largest exporting industries. Its exports contribute to the positive side of our trade balance. Agriculture can argue effectively that reservation of cargo for higher cost U.S. vessels can price their products out of an increasingly competitive world agricultural market, further exacerbating an already serious national balance-of-payments problem. Agriculture accounts for 15 percent of our export trade by value.

Also, it may be difficult to convince Congress and the President that our maritime industries need support. Our so-called big three liner carriers have been cited recently as examples of industrial health.

In evaluating the potential of unilateral cargo reservation, I believe we must avoid the contention that it represents an ultimate solution. There are no ultimate or enduring solutions. Political, social, and technical change is inevitable. We need an industrial policy capable of responding to that change. Cargo reservation based on legislative direction will lock us into a policy which like the Merchant Marine Act of 1936 we may never be able to shed.

What then should we do with respect to cargo policy in particular and merchant marine industrial policy in general? We need to create a variety of tools, of which cargo policy should be the tool of last resort; and even then it should be employed only in the form of bilateral agreements that preserve some form of competition.

From a practical viewpoint, I think we will see an increasing number of bilateral agreements in the next 10 years. These will have been entered into, generally, as a last resort to protect our national interest.

While bilateral agreements pose many of the same threats to the maritime industry and world trade as unilateral cargo reservation, they have many advantages that make them more desirable. Among these advantages are the following:

- They will be imposed in a slow and deliberative manner, and therefore will not shock the world trading community.
- They can be tailored to specific trades and countries, so they can be employed selectively and with flexibility.
- Bilateral treaties come to an end and can be refined and changed to meet changing conditions.
- Bilateral agreements will not be met with the same type of unified opposition that will be encountered with unilateral cargo reservation legislation.
- Bilateral agreements can be created to insure competition; competition provides mechanisms for keeping cost down and productivity up; and this in turn stimulates trade and improves the demand for ocean shipping.

A cargo policy based on a reluctant acquiescence to bilateral agreements cannot, of course, be the totality of our merchant marine industrial policy. Other steps, including selective government funding, must be employed to insure a viable merchant marine industry. Because the Federal Government uses the merchant marine as an instrument of national policy, it must be prepared to pay for the use. Government funding to insure a growing merchant fleet should not be called subsidy, but rather "user charges," in which the Government pays for the services it needs or perceives that it may need in the future.

U.S. merchant marine industrial policy must promote and assist new ventures into the industry, to insure that new innovative organizations are standing in line to fill the vacuums created by mature companies that fail or do not consistently advance the state of the art of cargo transportation.

In conclusion, cargo policy is not the ultimate answer or the enduring solution to the nation's seemingly endless search for a maritime industrial policy. Cargo policy, and in particular bilateral agreements, are valuable tools that can enhance an overall industrial policy. Merchant marine industrial policy itself must never again be encumbered by a single piece of inflexible legislation, but must instead be dynamic and flexible, consisting of many tools that can be applied with surgical precision.

PLENARY SESSION

December 4, 1984

SUMMARY OF DISCUSSION

Defense-Related Issues

During the second-day wrap-up session, most of the major maritime issues were discussed. National defense questions absorbed much of the time. Again, it was suggested that the shipbuilding segment of the industry should be funded by DOD, and that operators should not be saddled with the cost of defense features requirements. DOD should pay for the vessels it deems necessary for national security, but budgetary restrictions might make it necessary to fulfill requirements only for direct military support vessels (like Ro/Ros), and to forego construction of ships to support the civilian economy in wartime. Support for the commercial U.S. shipbuilding industry probably cannot be justified on economic grounds alone, since the market for new construction is so depressed and Far East shipyards are able to offer prices that are so much lower.

One suggestion that would aid U.S. shipbuilding without cost would be to set up foreign trade zones for ship construction, in the same manner as they now exist for automobile and other manufacturing. Components and raw materials are imported without duty, and the absence of duty results in lower delivered cost. A few foreign trade zones for ships have already been established. For the practice to become widespread, however, MarAd regulations on domestic content for ships built under Government tax deferral or loan guarantee programs would have to be changed.

The availability of crews for reserve fleet ships was again questioned. With a merchant fleet of perhaps only 100 ships and newer vessels requiring fewer crew members, the pool of shipboard labor may soon be inadequate.

A question raised as a possible topic of further study was whether DOD has adequately considered whether commercial ships are as useful as DOD-designed ships, or more so, for defense support purposes.

Maritime Objectives

A broader national security raised at the workshop issue concerned what part of the merchant fleet should be considered as supporting national security. While only some ships are useful in direct military support, it might be considered that we are in economic warfare with the Soviet bloc. The Soviets have already introduced ships that offer substantially below-market rates in both in U.S. and European trades. Their ability to dominate free world trade is clearly enhanced by the diminution of the U.S. fleet. Some

would argue that this is sufficient reason for Government support of the entire merchant marine.

There was agreement that the merchant marine should not be viewed as an economic end in itself, but as a support for trade and U.S. exports. Some workshop participants held that U.S.-flag ships are more reliable than foreign ships and, therefore, their use is beneficial to shippers. Other participants, notably the shippers, pointed out that for U.S. goods to be competitive in the marketplace, their price must be reasonable. Any increase in transportation costs, such as results when shippers are required by preference laws to use U.S. vessels that may be higher cost, reduces the competitiveness of U.S. products.

On this issue, there really was no resolution. Carriers continue to believe that cargo preference is important to them and that it benefits shippers as well by making carriage on some routes possible. Shippers generally believe that the lowest transportation cost provides the greatest benefit to them and their customers. Liner operators point out that their rates are fixed by conferences and are identical with the rates of foreign-flag conference members. However, it was also pointed out that conference rates are generally fixed to be compensatory to the highest cost operator, frequently the U.S. operator.

Government Regulation

There was agreement that excessive Government regulation has been detrimental to all sides. Foreign building is considered essential to profitable liner operations. Currently, unsubsidized operators who build abroad are discriminated against in cargo-preference regulations. Those vessels must wait 3 years before having equal eligibility to carry Government cargoes. At the same time, subsidized carriers were allowed (for 1 year only) to build abroad, and those vessels can carry preference cargoes and receive operating subsidies immediately. Some weaker companies seek to sell the Government their older vessels in order to raise capital to build modern ships abroad. Some participants supported legislation permitting foreign building as a high priority.

It was also noted that subsidized operators are forced to adhere to operational differential subsidy (ODS) regulations relating to essential trade routes, min-max sailings, etc.[36] While there has been effort on the part of MarAd to reduce the burden of such regulations, some participants felt they should be removed. Others felt that if they

36. These regulations require that the operator who receives subsidy payments maintain certain sailings on routes that are defined as essential to U.S. trade.

were removed, a reduction in subsidy amount would be appropriate. Some participants believed that U.S. liner operators can compete in operating costs in the international sphere with modern containerships, and that the Government should cease making this more difficult than necessary. Nonsubsidized carriers have advocated removal of ODS for foreign-built ships as a feasible way to phase out the ODS restrictions and Government direct subsidy in general. They believe this would bring all U.S.-flag carriers into an equitable promotional situation.

Bulk Cargo Issues

On the bulk side, the story is different. Commercial shippers appear to be reasonably satisfied with this foreign-flag market. A truly free market exists, and shippers can negotiate terms and choose whatever carriers they wish. There was agreement that any efforts to reduce the freedom of the bulk markets, such as imposition of an UNCTAD bulk code, should be firmly resisted. Shippers are also firmly opposed to any Government-imposed commercial cargo reservation, such as that in several recent legislative proposals.

Other Issues

The bright spot in U.S.-owned bulk carriage is the USEC fleet, and there was sentiment that the U.S. Government should support this foreign-flag fleet through reduced regulation and strong advocacy in international forums. The current attack on open registries in UNCTAD is a situation where the U.S. Government could support American-owned foreign-flag fleets.

Finally, one participant stated that there appears to be one area where U.S. industry could make inroads — neobulk shipping.[37] Neobulk trades (such as automobiles) have been increasing rapidly, while liner and regular bulk trades have been steady. The U.S.-flag fleet has not penetrated this trade at all. Yet the vessels are of a type where the United States has a comparative advantage — sophisticated, highly technological vessels. Most operations are now by European or Japanese fleets. No specific suggestions were given as to how the U.S. Government might support expansion into these trades. Further study may be warranted.

---

37. Trades where contract services are provided similar to bulk shipping practice but the commodities shipped are more of a general cargo type. Such commodities transported now in "ship-lots" are automobiles, logs, scrap steel, etc.